

EDWARDS LIFESCIENCES CORP  
Form S-3  
July 28, 2003

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As filed with the Securities and Exchange Commission on July 28, 2003

Registration No. 333-

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**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM S-3**

REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

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**EDWARDS LIFESCIENCES CORPORATION**

(Exact name of Registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**36-4316614**

(I.R.S. Employer Identification No.)

**One Edwards Way, Irvine, California 92614**  
**Telephone: (949) 250-2500**

(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

**Bruce P. Garren**  
**Edwards Lifesciences Corporation**  
**One Edwards Way**  
**Irvine, California 92614**  
**Telephone: (949) 250-2500**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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**Approximate date of commencement of proposed sale to the public:**  
**From time to time following the effectiveness of this registration statement.**

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box:

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box:

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If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. o

### CALCULATION OF REGISTRATION FEE

Title Of Each Class of Securities To Be Registered	Amount To Be Registered	Proposed Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
3.875% Convertible Senior Debentures due 2033	\$150,000,000	100%(1)(2)	\$150,000,000(1)(2)	\$12,135.00
Common Stock, par value \$1.00 per share(3)	2,744,238(4)	(5)	(5)	(5)

- (1) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457 (i) of the Securities Act of 1933, as amended.
- (2) Exclusive of accrued interest, if any.
- (3) Includes associated preferred stock purchase rights ("Rights") to purchase 1/100 of a share of Series A Junior Participating Preferred Stock, par value \$.01 per share, subject to adjustment. Rights initially are attached to and trade with the common stock of the Registrant and will not be exercisable until the occurrence of specified events.
- (4) Represents the number of shares of common stock that are initially issuable upon conversion of the 3.875% Convertible Senior Debentures due 2033 registered hereby. For purposes of estimating the number of shares of common stock issuable upon conversion of the debentures, the Registrant used a conversion price of \$54.66 per share of common stock. In addition to the shares set forth in the table, pursuant to Rule 416 under the Securities Act of 1933, as amended, the amount of common stock registered hereby also includes such indeterminate number of shares of common stock, including the associated Rights, as may be issuable from time to time upon conversion of the debentures as a result of stock splits, stock dividends and antidilution adjustments.
- (5) No additional consideration will be received for the common stock and, therefore, no registration fee is required pursuant to Rule 457(i).

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.

**Subject to completion, dated July 28, 2003**

**Information contained herein is subject to completion or amendment. A registration statement relating to these securities has been filed with the Securities and Exchange Commission. These securities may not be sold nor may offers to buy be accepted prior to the time the registration statement becomes effective. This prospectus is not an offer to sell the securities and it is not soliciting an offer to buy the securities in any state where the offer or sale is not permitted, nor shall there be any sale of these securities in any state in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such state.**

Prospectus

**\$150,000,000**

## **Edwards Lifesciences Corporation**

### **3.875% Convertible Senior Debentures due 2033 and the Common Stock Issuable Upon Conversion of the Debentures**

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We issued \$150,000,000 principal amount of our 3.875% Convertible Senior Debentures due 2033 in a private offering in May 2003. This prospectus will be used by selling securityholders to resell the debentures and the common stock issuable upon conversion of the debentures. We will not receive any proceeds from these resales.

We will pay interest on the debentures on May 15 and November 15, of each year, beginning on November 15, 2003. Beginning with the six-month interest period commencing on May 15, 2008, we will pay contingent interest during a six-month interest period if the average trading price of a debenture is above a specified level as described in this prospectus.

Holders may convert their debentures into shares of our common stock only under the following circumstances and to the following extent:

holders may convert their debentures, in whole or in part, during any calendar quarter (beginning with the quarter ending September 30, 2003) if, as of the last day of the preceding calendar quarter, the last reported sale price of our common stock on at least 20 trading days (whether or not consecutive) in the period of 30 consecutive trading days ending on the last trading day of such immediately preceding calendar quarter exceeds 120% of the applicable conversion price on the last trading day of such immediately preceding calendar quarter;

holders may convert any of their debentures (and only those debentures) that have been called for redemption; or

holders may convert their debentures, in whole or in part, upon the occurrence of specified corporate transactions described in this prospectus.

Holders may convert their debentures into shares of our common stock initially at a conversion price of \$54.66 per share of common stock (equivalent to an initial conversion rate of approximately 18.2949 shares of common stock per \$1,000 principal amount of debentures). The conversion price is subject to adjustment from time to time as described in this prospectus.

For United States federal income tax purposes, the debentures constitute contingent payment debt instruments. You should read the discussion under "Certain United States federal income tax considerations" beginning on page 52.

The debentures will mature on May 15, 2033. We may redeem for cash all or part of the debentures, at any time and from time to time, on or after May 15, 2008 at a redemption price equal to 100% of the principal amount of the debentures to be redeemed, plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the redemption date.

Holders of the debentures will have the right to require us to purchase all or a portion of their debentures at a price equal to 100% of the principal amount to be purchased, plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the purchase date, on May 15, 2008, May 15, 2013, and May 15, 2018. We will pay cash for all debentures so purchased on May 15, 2008. For any debentures purchased by us on May 15, 2013 or May 15, 2018, we may at our option choose to pay the purchase price for any such debentures in cash or in shares of our common stock or any combination thereof.

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If we undergo a Change in Control (as defined in this prospectus) prior to May 15, 2008, holders of the debentures will have the right to require us to purchase all or any portion of their debentures at a purchase price equal to 100% of the principal amount to be purchased, plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the purchase date. We may at our option choose to pay the purchase price for any debentures that holders require us to purchase upon a Change in Control in cash or in shares of our common stock or any combination thereof.

There is no public market for the debentures and we do not intend to apply for listing of the debentures on any securities exchange or for quotation of the debentures through any automated quotation system. The debentures currently trade in the Private Offerings, Resales and Trading through Automatic Linkages Market, commonly referred to as the PORTAL Market. However, once debentures are sold under this prospectus, those debentures will no longer trade on the PORTAL Market. Our common stock is listed on the New York Stock Exchange under the symbol "EW." The last reported sale price of our common stock on the New York Stock Exchange on July 25, 2003 was \$27.25 per share.

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**Investing in the debentures and the shares of common stock offered hereby involves risks. See "Risk factors" beginning on page 7 of this prospectus.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

The date of this prospectus is \_\_\_\_\_, 2003.

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You should rely only on the information contained or incorporated or deemed to be incorporated by reference in this prospectus. We have not authorized anyone to provide you with different information. Neither the debentures nor any shares of common stock issuable upon conversion of the debentures are being offered in any jurisdiction where the offer or sale is not permitted. The information contained in this prospectus speaks only as of the date of this prospectus and the information in the documents incorporated or deemed to be incorporated by reference in this prospectus speaks only as of the respective dates those documents were filed with the Securities and Exchange Commission (the "SEC").

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This prospectus contains summaries of certain provisions contained in some of the documents described herein, but reference is made to the actual documents for complete information. All of the summaries are qualified in their entirety by the actual documents. Copies of some of the documents referred to herein have been filed or incorporated by reference as exhibits to the registration statement of which this prospectus is a part and you may obtain copies of those documents as described below under "Available information" and "Incorporation of documents by reference."

## Summary

*This summary does not contain all of the information that may be important to you. You should read this entire prospectus and the documents incorporated and deemed to be incorporated by reference in this prospectus, including the financial statements and related notes, before making an investment decision. We sometimes refer to the offering being made by this prospectus as the "offering," we sometimes refer to the 3.875% convertible senior debentures due 2033 as the "debentures" and we sometimes refer to the persons who may offer or sell debentures or shares of common stock issued upon conversion of debentures pursuant to this prospectus as the "selling securityholders." Unless this prospectus indicates otherwise or the context otherwise requires, the terms "we," "our," "us" and "Edwards Lifesciences" refer to Edwards Lifesciences Corporation and its subsidiaries for periods on or after April 1, 2000 and to Baxter International Inc.'s CardioVascular Group for periods prior to April 1, 2000.*

### Edwards Lifesciences Corporation

**Overview.** We manufacture and sell products and technologies designed to treat advanced cardiovascular disease. We focus on providing products and technologies to address four main cardiovascular disease states: heart valve disease; coronary artery disease; peripheral vascular disease; and congestive heart failure. Our products and technologies that treat cardiovascular disease are categorized into the following five main areas:

*Cardiac surgery.* Our cardiac surgery portfolio is comprised primarily of products relating to heart valve therapy, transmyocardial revascularization, and cannulation used during open-heart surgery. We manufacture and sell tissue heart valves and repair products used to replace or repair a patient's diseased or defective heart valve.

*Critical care.* We manufacture and sell hemodynamic monitoring systems that are used to measure a patient's heart function in surgical and intensive care settings. Hemodynamic monitoring enables a clinician to balance the oxygen supply and demand of a critically ill patient and plays an important role in ensuring that the heart function of patients who have pre-existing cardiovascular conditions or other critical illnesses is optimized before they undergo a surgical procedure.

*Vascular.* We manufacture and sell a variety of products used to treat occlusive peripheral vascular disease, including a line of balloon-tipped, catheter-based products, surgical clips and inserts, angiography equipment, artificial implantable grafts, and an endovascular system used to treat abdominal aortic aneurysms less invasively than conventional surgical procedures.

*Perfusion.* We develop, manufacture and distribute, in regions outside the United States and Western Europe, a line of disposable products used during cardiopulmonary bypass procedures, including oxygenators, blood containers, filters and related devices.

*Other distributed products.* Other distributed products include sales of intra-aortic balloon pumps, pacemakers, angioplasty systems and other products sold through our distribution network in Japan, and miscellaneous pharmaceutical products sold in the United States.

Our principal executive offices are located at One Edwards Way, Irvine, California 92614. The telephone number at that address is (949) 250-2500.

**Corporate background.** Edwards Lifesciences was incorporated in Delaware on September 10, 1999 as a wholly owned subsidiary of Baxter International Inc. to assume the business and operations of Baxter's CardioVascular Group. Effective March 31, 2000, the business, assets and liabilities of Baxter's CardioVascular Group were transferred to Edwards Lifesciences and its subsidiaries and 100% of the common stock of Edwards Lifesciences was distributed to the stockholders of Baxter in a tax-free spin-off, which we sometimes refer to in this prospectus as the "Distribution." Since that time, Edwards Lifesciences has operated as an independent company.

**Recent developments.** On July 22, 2003, we announced our operating results for the second quarter ended June 30, 2003. Our second quarter consolidated net sales were \$217.8 million and our net income was \$21.1 million, or \$0.34 per diluted share. In the second quarter of 2002, our net sales were \$172.8 million with net income of \$30.6 million, or \$0.50 per diluted share.

**The offering**

Issuer	Edwards Lifesciences Corporation, a Delaware corporation.
Securities Offered	\$150 million aggregate principal amount of 3.875% Convertible Senior Debentures due 2033 and shares of our common stock issuable upon conversion of the debentures.
Maturity	May 15, 2033.
Interest	We will pay interest on the debentures semi-annually in arrears at an annual rate of 3.875%. The interest payment dates for the debentures are May 15 and November 15 of each year, commencing November 15, 2003.
Contingent Interest	Beginning with the six-month interest period commencing on May 15, 2008, we will pay contingent interest during a six-month interest period if the average trading price, as defined herein, of a debenture for the five trading days ending on and including the third trading day immediately preceding the first day of such six-month interest period equals or exceeds 120% of the principal amount of such debenture. The contingent interest payable per \$1,000 principal amount of a debenture in respect of any six-month interest period in which contingent interest is payable will accrue at the rate of 0.25% per six-month period of the average trading price per \$1,000 principal amount of such debenture for the applicable five trading day reference period ending on and including the third trading day immediately preceding the first day of such six-month interest period. For more information about contingent interest, see "Description of debentures Contingent interest."
Ranking	The debentures are our unsubordinated obligations and are not secured by any collateral. Your right to payment under the debentures is:
	effectively subordinated to the rights of our secured creditors, if any, to the extent of their security interests in our assets;
	equal with the rights of our creditors under our other unsecured, unsubordinated debt;
	senior to the rights of our creditors under any indebtedness we may issue in the future that is expressly subordinated to the debentures; and
	effectively subordinated to all existing and future indebtedness and other liabilities of our subsidiaries. In that regard, our primary bank credit facilities require that borrowings under

those facilities be guaranteed by domestic subsidiaries whose aggregate net revenues and aggregate net tangible assets equal or exceed 95% of our consolidated net revenues and consolidated net tangible assets.

At March 31, 2003, our consolidated subsidiaries had approximately \$349.2 million of outstanding indebtedness and other liabilities, excluding indebtedness and other liabilities owed to us or to other subsidiaries. See "Risk factors Risks related to the securities The debentures are effectively subordinated to the liabilities of our subsidiaries."

#### Conversion Rights

Holders may convert their debentures into shares of our common stock only under the following circumstances and to the following extent:

holders may convert their debentures, in whole or in part, during any calendar quarter (beginning with the quarter ending September 30, 2003) if, as of the last day of the preceding calendar quarter, the last reported sale price of our common stock on at least 20 trading days (whether or not consecutive) in the period of 30 consecutive trading days ending on the last trading day of such immediately preceding calendar quarter exceeds 120% of the applicable conversion price on the last trading day of such immediately preceding calendar quarter;

holders may convert any of their debentures (and only those debentures) that have been called for redemption; or

holders may convert their debentures, in whole or in part, upon the occurrence of specified corporate transactions described under "Description of the debentures Conversion rights Conversion upon specified corporate transactions."

Holders may convert their debentures into shares of our common stock initially at a conversion price, subject to adjustment as set forth herein, of \$54.66 per share of our common stock. This represents an initial conversion rate of approximately 18.2949 shares of our common stock per \$1,000 principal amount of debentures. As described in this

prospectus, the conversion price may be adjusted for certain reasons, but it will not be adjusted for accrued and unpaid interest or contingent interest, if any. You will not receive any cash payment representing accrued and unpaid interest or contingent interest, if any, upon conversion of a debenture.

Optional Redemption

We may, at our option, redeem for cash all or part of the debentures, at any time and from time to time, on or after May 15, 2008, for a price equal to 100% of the principal amount of the debentures to be redeemed, plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the redemption date.

Purchase of Debentures by Us at the Option of the Holder

You have the right to require us to purchase all or a portion of your debentures on May 15, 2008, May 15, 2013 and May 15, 2018 (each, a "purchase date"). In each case, the purchase price payable will be equal to 100% of the principal amount of the debentures to be purchased plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the purchase date. Any debentures we purchase on May 15, 2008 will be paid for in cash. For any debentures purchased by us on May 15, 2013 or May 15, 2018, we may, at our option, pay the purchase price in cash or shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder") or a combination of cash and shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder"), provided that we will pay accrued and unpaid interest, if any, and contingent interest, if any, in cash.

Purchase of Debentures by Us at Option of Holder upon Change in Control

If we undergo a Change in Control (as defined in this prospectus) prior to May 15, 2008, you will have the right, at your option, to require us to purchase all or any portion of your debentures. The Change in Control purchase price will be equal to 100% of the principal amount of the debentures to be purchased plus any accrued and unpaid interest and contingent interest, if any, to, but excluding, the Change in Control purchase date. We may, at our option, pay the Change in Control purchase price for such debentures in cash or shares of our common stock (valued using the method set forth

in "Description of the debentures Purchase of debentures by us at the option of the holder") or a combination of cash and shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder"), provided that we will pay accrued and unpaid interest, if any, and contingent interest, if any, in cash.

U.S. Federal Income Taxation

The debentures constitute contingent payment debt instruments for U.S. federal income tax purposes, and are subject to U.S. federal income tax regulations applicable to contingent payment debt instruments. Based on that treatment, holders of the debentures generally are required to accrue interest income on the debentures, which we refer to as tax original issue discount, in the manner described in this prospectus, regardless of whether the holder uses the cash or accrual



method of tax accounting. You will be required, in general, to include tax original issue discount in income based on the rate at which we would issue a noncontingent, nonconvertible, fixed-rate debt instrument with terms and conditions otherwise similar to those of the debentures, which rate is expected to exceed the stated interest on the debentures. Accordingly, it is expected that you will be required to include interest in taxable income each year in excess of the accruals on the debentures for non-tax purposes (i.e., in excess of the stated semi-annual regular interest payments and any contingent interest payments) actually received in that year. Furthermore, upon a sale, purchase by us at your option, exchange, conversion or redemption of the debentures, you will recognize gain or loss equal to the difference between your amount realized and your adjusted tax basis in the debentures. The amount realized by you will include the fair market value of any common stock you receive. Any gain recognized on a sale, purchase by us at your option, exchange, conversion, or redemption of the debentures will be treated as ordinary interest income. You should consult your tax advisor as to the U.S. federal, state, local or other tax consequences, as well as any foreign tax consequences, of acquiring, owning, and disposing of the debentures. See "Certain United States federal income tax considerations."

Registration Rights

Pursuant to a registration rights agreement that we entered into in connection with the private offering

of the debentures in May 2003, we have filed a shelf registration statement under the Securities Act of 1933 relating to the resale of the debentures and the common stock issuable upon conversion of the debentures. This prospectus constitutes a part of that registration statement. We filed the shelf registration statement solely to permit the resale of debentures issued in the May 2003 private offering and shares of common stock issued on conversion of those debentures, and investors who purchase debentures or shares of common stock from selling securityholders in this offering will not be entitled to any registration rights under the registration rights agreement. In addition, under the registration rights agreement, selling securityholders may be required to discontinue the sale or other disposition of debentures and shares of common stock issued upon conversion of debentures pursuant to the shelf registration statement and to

discontinue the use of this prospectus under certain circumstances specified in the registration rights agreement.

Use of Proceeds

We will not receive any of the proceeds from the sale by the selling securityholders of debentures or shares of common stock issued upon conversion of debentures.

Book-Entry Form

The debentures were issued in book-entry form and are represented by permanent global certificates without interest coupons, deposited with, or on behalf of, The Depository Trust Company, or "DTC," and registered in the name of a nominee of DTC. Beneficial interests in the debentures are shown on, and transfers are effected only through, records maintained by DTC or its nominee and any such interest may not be exchanged for certificated debentures, except in limited circumstances.

Trading

There is no public market for the debentures and we do not intend to apply for listing of the debentures on any securities exchange or for quotation of the debentures through any automated quotation system. The debentures currently trade in the PORTAL Market. However, once debentures are sold under this prospectus, those debentures will no longer trade on the PORTAL Market. No assurance can be given that a trading market for the debentures will exist or as to the liquidity of any trading market for the debentures that may exist. Our common stock is listed on the New York Stock Exchange under the symbol "EW."

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**Risk factors**

*You should carefully consider the risks described below, as well as other information contained in this prospectus and the documents incorporated or deemed to be incorporated by reference in this prospectus, before buying any of the debentures or shares of common stock offered by this prospectus. If any of the events described below occurs, our business, financial condition or results of operations could be materially harmed. In that case, the value of the debentures and the market price of our common stock could decline and you may lose part or all of your investment.*

**Risks related to our business**

*If we do not introduce new products in a timely manner, our products may become obsolete, and our operating results may suffer.*

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The cardiovascular products industry is characterized by rapid technological changes, frequent new product introductions and evolving industry standards. Without the timely introduction of new products and enhancements, our products will likely become technologically obsolete over time, in which case our revenue and operating results would suffer. Even if we are able to develop new technologies, these technologies may not be accepted quickly because of industry-specific factors, such as the need for regulatory clearance, unanticipated restrictions imposed on approved indications, entrenched patterns of clinical practice and uncertainty over third-party reimbursement.

Moreover, significant technical innovations generally will require a substantial investment before we can determine the commercial viability of these innovations. We may not have the financial resources necessary to fund these technical innovations. In addition, even if we are able to successfully develop enhancements or new generations of our products, these enhancements or new generations of products may not produce revenue in excess of the costs of development, and they may be quickly rendered obsolete by changing customer preferences or the introduction by our competitors of products embodying new technologies or features.

***We may incur product liability losses that could adversely affect our operating results.***

Our business exposes us to potential product liability risks that are inherent in the design, manufacture and marketing of medical devices. Our products are often used in surgical and intensive care settings with seriously ill patients. In addition, some of the medical devices manufactured and sold by us are designed to be implanted in the human body for long periods of time. We could be the subject of product liability suits alleging that component failures, manufacturing flaws, design defects or inadequate disclosure of product-related risks or product-related information could result in an unsafe condition or injury to patients. Product liability lawsuits and claims, safety alerts or product recalls in the future, regardless of their ultimate outcome, could have a material adverse effect on our business and reputation and on our ability to attract and retain customers.

***We may experience supply interruptions that could harm our ability to manufacture products.***

We use a diverse and broad range of raw and organic materials and other items in the design and manufacture of our products. Our non-implantable products are manufactured from man-made raw materials including resins, chemicals, electronics and metals. Our heart valve therapy products are manufactured from treated natural animal tissue and man-made materials. We purchase certain of the materials and components used in the manufacture of our products from external suppliers. In addition, we purchase certain supplies from single sources for reasons of quality assurance, cost-effectiveness or constraints resulting from regulatory requirements. We work closely with our suppliers to assure continuity of supply while maintaining high quality and reliability. Alternative supplier options are generally considered and identified, although we do not typically pursue regulatory qualification of alternative sources due to the strength of our existing supplier relationships and the

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time and expense associated with this regulatory process. Although a change in suppliers could require significant effort or investment by us in circumstances where the items supplied are integral to the performance of our products or incorporate unique technology, management does not believe that the loss of any existing supply contract would have a material adverse effect on us.

In an effort to reduce potential product liability exposure, in the past certain suppliers have announced that they might limit or terminate sales of certain materials and parts to companies that manufacture implantable medical devices. In some cases, we have been required to indemnify suppliers for product liability expenses in order to continue to receive materials or parts. There can be no assurance that an indemnity from us will be satisfactory to these suppliers in the future. If we are unable to obtain these raw materials or there is a significant increase in the price of materials or components, our business could be harmed.

***We may be required to recognize additional charges in connection with the write-down of some of our investments, the disposition of some of our businesses or for other reasons.***

We have made investments in the equity instruments of other companies, and may make further such investments in the future. To the extent that the value of any such investment declines, we may be required to recognize charges to write down the value of that investment. For example, in September 2002, we recorded a \$67.4 million pretax charge related to the impairment of our investment in the preferred stock of World Heart Corporation. See "Disposition of assets and other non-recurring charges, net" under "Management's discussion and analysis of financial condition and results of operations" in our Annual Report on Form 10-K for the year ended December 31, 2002.

In the case of some of the companies in which we have invested, the value of their equity securities has declined since the time of our original investment. As a result, we may be required to recognize additional charges, which could be substantial, to write down our investments. At December 31, 2002, in addition to our investment in World Heart, which was \$6.1 million, we had approximately \$17.4 million of

investments in equity instruments of other companies and had recorded unrealized losses on these investments of approximately \$6.8 million, net of tax, on our balance sheet under "accumulated other comprehensive income."

As part of the ongoing evaluation of our various businesses and product lines, we from time to time identify businesses or product lines that are not performing at a level commensurate with the rest of our business. We may from time to time seek to dispose of these underperforming businesses or product lines, and may also seek to dispose of businesses or product lines from time to time for strategic or other business reasons. If we are unable to dispose of a business or product line on terms we consider acceptable, we may voluntarily terminate that business or cease providing that product. Any of these events may result in charges, which could be substantial and which could adversely affect our results of operations.

We have entered into interest rate swap agreements in connection with some of our indebtedness, and expect that we will continue to do so from time to time in the future. In the event that we elect to terminate a swap agreement prior to its maturity, we may be required to make cash payments to the counterparty and to recognize a charge in connection with that termination, which could adversely affect our results of operations.

***We may not successfully identify and complete acquisitions or strategic alliances on favorable terms or achieve anticipated synergies relating to any acquisitions or alliances.***

As part of our growth strategy, we regularly review potential acquisitions of complementary businesses, technologies, services or products and potential strategic alliances. We may be unable to find suitable acquisition candidates or appropriate partners with which to form partnerships or strategic alliances. Even if we identify appropriate acquisition or alliance candidates, we may be unable to

complete such acquisitions or alliances on favorable terms, if at all. In addition, the process of integrating an acquired business, technology, service or product into our existing business and operations may result in unforeseen operating difficulties and expenditures. Integration of an acquired company also may require significant management resources that otherwise would be available for ongoing development of our business. Moreover, we may not realize the anticipated benefits of any acquisition or strategic alliance, and such transactions may not generate anticipated financial results. In addition, we may be required to take charges or write-downs in connection with acquisitions we have made or may make in the future. Future acquisitions could also require issuances of equity securities, the incurrence of debt, contingent liabilities or amortization expenses related to other intangible assets, any of which could harm our business.

***Our business is subject to economic, political and other risks associated with international sales and operations.***

Because we sell our products in a number of foreign countries, our business is subject to risks associated with doing business internationally. Our net sales originating outside of the United States, as a percentage of total net sales, were 45.6% in 2002. We anticipate that sales from international operations will continue to represent a substantial portion of our total sales. In addition, many of our manufacturing facilities and suppliers are located outside of the United States. Our management expects to increase our sales efforts internationally, which could expose us to greater risks associated with international sales and operations. Accordingly, our future results could be harmed by a variety of factors, including:

changes in foreign medical reimbursement policies and programs;

unexpected changes in foreign regulatory requirements;

changes in foreign currency exchange rates;

changes in a specific country's or region's political or economic conditions, particularly in emerging regions;

trade protection measures and import or export licensing requirements;

potentially negative consequences from changes in tax laws;

difficulty in staffing and managing foreign operations;

changes in the international political situation;

differing labor regulations; and

differing protection of intellectual property.

***We are subject to risks arising from currency exchange rate fluctuations.***

We generated 45.6% of our 2002 net sales outside of the United States. Substantially all of our sales outside of the United States are denominated in local currencies. Measured in local currency, a substantial portion of our foreign generated sales were generated in Europe (and primarily denominated in the Euro) and in Japan. The United States dollar value of our foreign-generated sales varies with currency exchange rate fluctuations. Significant increases in the value of the United States dollar relative to the Euro or the Japanese yen, as well as other currencies, could have a material adverse effect on our results of operations. We have a hedging policy that attempts to manage currency exchange rate risks to an acceptable level based on management's judgment of the appropriate trade-off between risk, opportunity and cost; however, this hedging policy does not completely eliminate the effects of currency exchange rate fluctuations.

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***Fluctuations in our quarterly operating results may cause our stock price to decline.***

Our sales and operating results may vary significantly from quarter to quarter. A high proportion of our costs are fixed, due in part to significant sales, research and development and manufacturing costs. Thus, small declines in revenue could disproportionately affect operating results in a quarter, and the price of our common stock may fall, which could in turn adversely affect the value of the debentures. Other factors that could affect quarterly operating results include:

demand for and clinical acceptance of products;

the timing and execution of customer contracts, particularly large contracts that would materially affect our operating results in a given quarter;

the timing of sales of products;

changes in foreign currency exchange rates;

unanticipated delays or problems in introducing new products;

competitors' announcements of new products, services or technological innovations;

changes in our pricing policies or the pricing policies of our competitors;

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increased expenses, whether related to sales and marketing, raw materials or supplies, product development or administration;

adverse changes in the level of economic activity in the United States and other major regions in which we do business;

costs related to possible acquisitions of technologies or businesses;

our ability to expand our operations; and

the amount and timing of expenditures related to expansion of our operations.

### ***Our inability to protect our intellectual property could have a material adverse effect on our business.***

Our success and competitive position are dependent, in part, upon our proprietary intellectual property. We rely on a combination of patents, trade secrets and nondisclosure agreements to protect our proprietary intellectual property, and will continue to do so. Although we seek to protect our proprietary rights through a variety of means, we cannot guarantee that the protective steps we have taken are adequate to protect these rights. Patents issued to or licensed by us in the past or in the future may be challenged and held invalid or not infringed by third parties. Competitors may also challenge our patents. In addition, certain of our patents are due to expire within the next six years and we may be unsuccessful in our efforts to extend these patents through improvement patents, modifications or line extensions. The failure to maintain our patents could have a material adverse effect on us.

We also rely on confidentiality agreements with certain employees, consultants and other parties to protect, in part, trade secrets and other proprietary information. These agreements could be breached and we may not have adequate remedies for any breach. In addition, others may independently develop substantially equivalent proprietary information or gain access to our trade secrets or proprietary information. We spend significant resources to monitor and enforce our intellectual property rights. However, we may not be able to detect infringement and may lose our competitive position in the industry. In addition, competitors may design around our technology or develop competing technologies. Intellectual property rights may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture increased market position.

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### ***Third parties may claim we are infringing their intellectual property, and we could suffer significant litigation or licensing expenses or be prevented from selling products.***

During recent years, our competitors have been involved in substantial litigation regarding patent and other intellectual property rights in the medical device industry generally. In the future, we may be forced to defend ourselves against other claims and legal actions alleging infringement of the intellectual property rights of others. Because intellectual property litigation can be costly and time consuming, our intellectual property litigation expenses could be significant. Adverse determinations in any such litigation could subject us to significant liabilities to third parties, could require us to seek licenses from third parties and could, if such licenses are not available, prevent us from manufacturing, selling or using certain of our products, any one of which could have a material adverse effect on us.

Third parties could also obtain patents that may require us to either redesign our products or, if possible, negotiate licenses to conduct our business. If we are unable to redesign our products or obtain a license, we may have to exit a particular product offering.

### ***We face intense competition and consolidation within our industry, and if we do not compete effectively, our business will be harmed.***

The cardiovascular medical device industry is highly competitive. We compete with many companies, some of which have longer operating histories, better brand or name recognition and greater access to financial and other resources than us. Furthermore, the industry is characterized by intensive development efforts and rapidly advancing technology. Our present and future products could be rendered obsolete or uneconomical by technological advances by one or more of our current or future competitors or by alternative therapies, including drug therapies. See "Business Competition" in our Annual Report on Form 10-K for the year ended December 31, 2002. Our future success will depend, in large part, on our ability to develop and acquire new products and technologies, anticipate technology advances and keep pace with other developers of cardiovascular therapies and technologies.

The medical device industry has been consolidating and as a result, transactions with customers are larger, more complex and tend to involve more long-term contracts. The enhanced purchasing power of these larger customers may also increase downward pressure on product pricing. In addition, many existing and potential domestic customers for our products have combined to form group purchasing organizations, or "GPOs." GPOs negotiate pricing arrangements with medical supply manufacturers and distributors and these negotiated prices are made available to members of GPOs. If we are not one of the providers selected by a GPO, we may be precluded from making sales to members of a GPO for several years. Even if we are one of the selected providers, we may be at a disadvantage relative to other selected providers that are able to offer volume discounts based on purchases of a broader range of medical equipment and supplies. Further, we may be required to commit to pricing that has a material adverse effect on our sales and profit margins, business, financial condition and results of operations.

***We and our customers are subject to various governmental regulations, and we may incur significant expenses to comply with these regulations and develop our products to be compatible with these regulations.***

The medical devices manufactured and marketed by us are subject to rigorous regulation by the U.S. Food and Drug Administration, or "FDA," and numerous other federal, state and foreign governmental authorities. The process of obtaining regulatory approvals to market a medical device, particularly from the FDA and certain foreign governmental authorities, can be costly and time consuming, and approvals might not be granted for future products on a timely basis, if at all. Delays in receipt of, or failure to obtain, approvals for future products could result in delayed realization of product revenues or in substantial additional costs, which could have material adverse effects on our business or results of operations. In addition, there can be no assurance that we will be or will continue to be in compliance with applicable FDA and other material regulatory requirements. If the FDA were

to conclude that we were not in compliance with applicable laws or regulations, it could institute proceedings to detain or seize our products, issue a recall, impose operating restrictions, enjoin future violations and assess civil penalties against us, our officers or our employees and could recommend criminal prosecution to the Department of Justice. Moreover, the FDA could proceed to ban, or request recall, repair, replacement or refund of the cost of, any device or product manufactured or distributed by us. Furthermore, both the FDA and foreign government regulators have become increasingly stringent, and we may be subject to more rigorous regulation by governmental authorities in the future.

***We are subject to risks arising from concerns and/or regulatory actions relating to "mad cow disease."***

Certain of our products, including pericardial tissue valve products, are manufactured using bovine tissue. Concerns relating to the potential transmission of bovine spongiform encephalopathy, or "BSE," commonly known as "mad cow disease," from cows to humans may result in reduced acceptance in certain geographies of bovine products. In addition, various governmental bodies are considering stricter regulation of such products. We obtain our bovine tissue only from sources within the United States, where strong control measures and surveillance programs exist and where no BSE cases have been reported. In addition, the bovine tissue used in our pericardial tissue valve products are from tissue types considered by global health and regulatory organizations to have shown no risk of infectibility. We have not experienced any adverse impact on our sales as a result of concerns regarding BSE, but no assurance can be given that such an impact may not occur in the future.

***If third-party payors decline to reimburse our customers for our products or reduce reimbursement levels, our ability to profitably sell our products will be harmed.***

We sell our products and technologies to hospitals, doctors and other health care providers, all of which receive reimbursement for the health care services provided to their patients from third-party payors, such as government programs (both domestic and international), private insurance plans and managed care programs. These third-party payors may deny reimbursement if they determine that a device used in a procedure was not used in accordance with cost-effective treatment methods as determined by such third-party payor, or was used for an unapproved indication. Third-party payors may also decline to reimburse for experimental procedures and devices. We believe that many of our existing and future products are cost-effective because they are intended to reduce overall health care costs over a long period of time. We cannot be certain whether these third-party payors will recognize these cost savings or will merely focus on the lower initial costs associated with competing therapies. If our products are not considered cost-effective by third-party payors, our customers may not be reimbursed for our products.

In addition, third-party payors are increasingly attempting to contain health care costs by limiting both coverage and the level of reimbursement for medical products and services. There can be no assurance that levels of reimbursement, if any, will not be decreased in the future, or that future legislation, regulation or reimbursement policies of third-party payors will not otherwise adversely affect the demand for and price levels of our products. In Japan, customers are reimbursed for our products under a government-operated insurance system. Under this system, the Japanese government annually reviews the reimbursement levels for products. The Japanese government is also considering other

reimbursement regulation. If the Japanese government decides to reduce reimbursement levels for our products, our product pricing may be adversely affected.

***We are, or may be, subject to lawsuits related to products or services manufactured or performed by us.***

We are, or may be, a party to, or may be otherwise responsible for, pending or threatened lawsuits or other claims related to products and services currently or formerly manufactured or performed, as applicable, by us or other matters. Such cases and claims may raise difficult and complex factual and

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legal issues and may be subject to many uncertainties and complexities, including, but not limited to, the facts and circumstances of each particular case or claim, the jurisdiction in which each suit is brought, and differences in applicable law. Upon resolution of any pending legal matters or other claims, we may incur charges in excess of presently established reserves. While such a charge could have a material adverse impact on our net income or net cash flows in the period in which it is recorded or paid, management believes that no such charge relating to any currently pending lawsuit would have a material adverse effect on our consolidated financial position.

***The market price for our common stock may be volatile.***

The market price of our common stock could fluctuate substantially in the future in response to a number of factors, including the following:

quarterly variations in operating results, as discussed above under " Fluctuations in our quarterly operating results may cause our stock price to decline,"

announcements of innovations, new products, strategic developments or business combinations by us or our competitors,

changes in our expected operating expense levels or income and losses,

changes in financial estimates and recommendations of securities analysts,

the operating and securities price performance of other companies that investors may deem comparable to us, and

changes in general conditions in the economy, the financial markets, the domestic or international political situation, particularly in light of the conflict in Iraq, or the medical device industry.

In addition, in recent years the stock market has experienced extreme price and volume fluctuations. This volatility has had a significant effect on the market prices of securities issued by many companies for reasons unrelated to their operating performance. These broad market fluctuations may materially adversely affect our stock price, regardless of our operating results.

***Our stockholder rights plan, charter and bylaws, as well as provisions of Delaware law, could make it difficult for a third party to acquire our company.***

We have a stockholder rights plan that may have the effect of discouraging unsolicited takeover proposals. The rights issued under the stockholder rights plan would cause substantial dilution to a person or group that attempts to acquire us on terms not approved in advance by our board of directors. In addition, Delaware corporate law and our charter and bylaws contain provisions that could delay, deter or prevent a change in control of our company or our management. These provisions could also discourage proxy contests and make it more difficult for our stockholders to elect directors and take other corporate actions without the concurrence of our management or board of directors. These provisions:



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authorize our board of directors to issue "blank check" preferred stock, which is preferred stock that can be created and issued by our board of directors, without stockholder approval, with rights senior to those of common stock;

provide for a staggered board of directors and three-year terms for directors, so that no more than one-third of our directors could be replaced at any annual meeting;

provide that directors may be removed only for cause;

provide that stockholder action may be taken only at a special or regular meeting and not by written consent;

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provide for super-majority voting requirements for some provisions of our charter; and

establish advance notice requirements for submitting nominations for election to the board of directors and for proposing matters that can be acted upon by stockholders at a meeting.

We are also subject to anti-takeover provisions under Delaware law, which could also delay or prevent a change of control. For information about these provisions and laws, see "Description of capital stock" in this prospectus. Together, these provisions of our charter and bylaws, Delaware law and our stockholder rights plan may discourage transactions that otherwise could provide for the payment of a premium over prevailing market prices of our common stock and, possibly, the debentures, and also could limit the price that investors are willing to pay in the future for shares of our common stock and the debentures.

***Our issuance of preferred stock could adversely affect holders of our common stock and the debentures and discourage a takeover.***

Our board of directors is authorized to issue up to 50,000,000 shares of preferred stock without any action on the part of our stockholders. Our board of directors also has the power, without stockholder approval, to set the terms of any series of preferred stock that may be issued, including voting rights, dividend rights, preferences over our common stock with respect to dividends or in the event of a dissolution, liquidation or winding up and other terms. In the event that we issue preferred stock in the future that has preference over our common stock with respect to payment of dividends or upon our liquidation, dissolution or winding up, or if we issue preferred stock with voting rights that dilute the voting power of our common stock, the rights of the holders of our common stock or the market price of our common stock and, possibly, the value of the debentures could be adversely affected. In addition, the ability of our board of directors to issue shares of preferred stock without any action on the part of our stockholders may impede a takeover of us and prevent a transaction favorable to the holders of our common stock and the debentures.

### **Risks related to the securities**

***Future sales of our common stock in the public market could adversely affect the trading price of our common stock and the value of the debentures and our ability to raise funds in new stock offerings.***

Future sales of substantial amounts of our common stock in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and the value of the debentures and could impair our ability to raise capital through future offerings of equity or equity-related securities. As of March 31, 2003, we had

60,396,796 shares of common stock outstanding,

9,177,956 shares of common stock reserved for issuance upon exercise of options outstanding under our stock option plans with a weighted average exercise price of \$18.42 per share and

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in addition to the shares reserved for issuance upon the exercise of options referred to in the preceding bullet point, 3,610,387 additional shares reserved for future issuance under stock option plans and employee stock purchase plans.

In addition, at our annual meeting of stockholders on May 14, 2003, our stockholders approved of an amendment to our Long-Term Stock Incentive Compensation Program, which amendment increased the number of shares of common stock authorized for issuance under that program by 3,000,000 shares, from 12,500,000 shares to 15,500,000 shares.

No prediction can be made as to the effect, if any, that future sales of shares of common stock or the availability of shares of common stock for future sale, will have on the trading price of our common stock or the value of the debentures prevailing from time to time. Sales of substantial

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amounts of common stock (including shares issued upon the exercise of stock options, upon conversion of the debentures or, under the circumstances described in the following paragraph, upon repurchase by us of debentures), or the perception that such sales could occur, may adversely affect prevailing market prices for our common stock and the value of the debentures.

The debentures will be convertible at the option of the holders into shares of our common stock, subject to the conditions described under "Description of the debentures Conversion rights." We have registered the debentures and the shares of common stock issuable upon conversion of the debentures pursuant to a registration statement filed with the SEC of which this prospectus is a part. Accordingly, any shares of common stock issued on conversion of the debentures and subsequently sold pursuant to the registration statement will be freely tradable in the public markets without restriction. In addition, if we are required to repurchase debentures following specified change in control events relating to us as described below under "Description of the debentures Purchase of debentures by us at option of holder upon a Change in Control," we will have the option of paying the purchase price either in cash or in shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder") or both; provided that we will be required to pay any accrued interest and contingent interest, if any, in cash. Likewise, holders may require us to purchase all or a portion of their debentures on May 15, 2008, May 15, 2013 and May 15, 2018 as described below under "Description of the debentures Purchase of debentures by us at the option of the holder," in which case we will also have the option, except in the case of the purchase in year 2008, of paying the purchase price either in cash or in shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder") or both; provided that we will be required to pay any accrued interest and contingent interest, if any, in cash. The conversion of debentures into common stock or the issuance of common stock to pay the purchase price of any debentures could result in the issuance of a substantial number of shares and substantial dilution to our stockholders.

We have agreed, with certain exceptions, not to sell or otherwise transfer any shares of our common stock for 90 days after May 6, 2003 without first obtaining the written consent of J.P. Morgan Securities Inc. With this consent, we may sell shares before the expiration of such period without prior notice to our other stockholders or to any public market in which our common stock trades.

### ***We may be unable to repurchase debentures at the option of the holders and in other circumstances.***

Upon the occurrence of specified kinds of change in control events relating to us, holders of the debentures being offered hereby may, at their option, require us to repurchase all or a portion of their debentures at a price of 100% of the principal amount, plus accrued interest, if any, and contingent interest, if any, payable at our option in cash or in shares of our common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder") or both; provided that we will be required to pay any accrued interest and contingent interest, if any, in cash. In addition, holders may require us to purchase all or a portion of their debentures on May 15, 2008, May 15, 2013 and May 15, 2018 a price equal to 100% of the principal amount, plus accrued interest, if any, and contingent interest, if any, payable, in the case of the purchase in year 2008, in cash and, in the case of any purchase in the subsequent years, at our option in cash or in shares of common stock (valued using the method set forth in "Description of the debentures Purchase of debentures by us at the option of the holder") or both; provided that we will be required to pay any accrued interest and contingent interest, if any, in cash. See "Description of the debentures Purchase of debentures by us at the option of the holder upon Change in Control" and " Purchase of debentures by us at the option of the holder."

We are currently a party to an unsecured revolving credit agreement providing for aggregate borrowings of up to \$430 million and expiring on March 30, 2005 (the "Five Year Credit Facility") and a second unsecured revolving credit facility providing for aggregate borrowings of up to \$100 million

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and expiring on March 25, 2004 (the "364 Day Facility" and, together with the Five Year Credit Facility, the "Credit Facilities"). We are also a party to two securitization facilities, one dollar-denominated (the "U.S. Receivables Facility") and one yen-denominated (the "Japan Receivables Facility") whereby we are permitted to sell undivided interests in certain eligible pools of trade accounts receivable in an aggregate amount of up to \$40 million under the U.S. Receivables Facility and six billion yen (or approximately \$50.1 million based on currency exchange rates in effect on March 31, 2003) under the Japan Receivables Facility. The Japan Receivables Facility expires on December 3, 2005 and the U.S. Receivables Facility expires in December 2003. Certain change in control events may constitute or otherwise result in events of default under our Credit Facilities, our U.S. Receivables Facility and other instruments and agreements to which we and our subsidiaries are or may in the future become a party. These events of default could result in borrowings outstanding and other amounts due under our Credit Facilities, the U.S. Receivables Facility and any such other instruments and agreements becoming immediately due and payable. We cannot assure you that we would have the financial resources or otherwise be able to arrange financing to pay the amounts that may become due if we are required to purchase the debentures for cash under the circumstances described above or if our obligations under the Credit Facilities, the U.S. Receivables Facility or these or other instruments or agreements were accelerated.

***Our holding company structure may adversely affect our ability to meet our debt service obligations under the debentures.***

Substantially all of our consolidated assets are held by our subsidiaries. Accordingly, our cash flow and our ability to service our debt, including the debentures, depends on the results of operations of our subsidiaries and upon the ability of our subsidiaries to provide us cash, whether in the form of dividends, loans or otherwise, to pay amounts due on our obligations, including the debentures. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to make payments on the debentures or to make any funds available for that purpose. In addition, dividends, loans or other distributions from our subsidiaries to us may be subject to contractual and other restrictions, are dependent upon the results of operations of our subsidiaries, may be subject to tax or other laws limiting our ability to repatriate funds from foreign subsidiaries, and are subject to other business considerations.

***The debentures are effectively subordinated to the liabilities of our subsidiaries.***

Because of our holding company structure, the debentures are effectively subordinated to all existing and future liabilities of our subsidiaries. These liabilities may include indebtedness, trade payables, guarantees, lease obligations and letter of credit obligations. Therefore, our rights and the rights of our creditors, including the holders of the debentures, to participate in the assets of any subsidiary upon that subsidiary's liquidation or reorganization will be subject to the prior claims of the subsidiary's creditors and of the holders of any indebtedness or other obligations guaranteed by that subsidiary, except to the extent that we may ourselves be a creditor with recognized claims against the subsidiary. However, even if we are a creditor of one of our subsidiaries, our claims would still be effectively subordinated to any security interests in, or mortgages or other liens on, the assets of that subsidiary and would be subordinate to any indebtedness of the subsidiary senior to that held by us. Although some of our debt instruments impose limitations on the incurrence of additional indebtedness, our subsidiaries retain the ability to incur substantial additional indebtedness and other obligations.

As discussed above, we have a \$430 million Five Year Credit Facility and a \$100 million 364 Day Facility. The Five Year Credit Facility permits borrowings to be made by both Edwards Lifesciences Corporation and some of its subsidiaries. As of March 31, 2003, we had total borrowings of approximately \$276.9 million outstanding under the Five Year Credit Facility and no borrowings outstanding under the 364 Day Facility. Of the borrowings outstanding under the Five Year Credit

Facility, \$116.0 million had been borrowed by Edwards Lifesciences Corporation and \$160.9 million had been borrowed by some of its subsidiaries. Edwards Lifesciences Corporation has guaranteed the borrowings by its subsidiaries under the Five Year Credit Facility.

At March 31, 2003, our consolidated subsidiaries had approximately \$349.2 million of outstanding indebtedness and other liabilities, excluding indebtedness and other liabilities owed to us or to other subsidiaries but including \$160.9 million of borrowings under the Five Year Credit Facility. In addition, our Credit Facilities require that domestic subsidiaries whose aggregate net revenue and aggregate net tangible assets equal or exceed 95% of our consolidated net revenues and consolidated net tangible assets, as defined under the Credit Facilities, respectively, guarantee all borrowings, letters of credit and other obligations under our Credit Facilities, including, in the case of the Five Year Credit Facility, borrowings and other obligations of our subsidiaries under the Five Year Credit Facility. In addition, at December 31, 2002 our consolidated subsidiaries were obligated under operating lease agreements to make future minimum lease payments aggregating approximately \$18.5 million through 2007. See "Management's discussion and analysis of financial condition and results of operations Liquidity and capital resources."

***The debentures are not protected by restrictive covenants.***

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The indenture governing the debentures does not contain any financial or operating covenants or restrictions on the payments of dividends, the incurrence of indebtedness or other liabilities or the issuance or repurchase of securities by us or any of our subsidiaries. Although some of our other debt instruments impose limitations on our incurrence of additional indebtedness, we retain the ability to incur substantial additional indebtedness and other obligations. Any significant amounts of additional indebtedness or other obligations that we incur in the future may harm our ability to service our indebtedness, including the debentures, and pay our other obligations. Although the holders of the debentures will have the right, upon the occurrence of specified kinds of change in control events, to require us to repurchase all or a portion of their debentures, there can be no assurance that this right will afford protection to holders of the debentures in the event of a business combination, highly leveraged transaction or change of control event affecting us.

### ***We have increased our indebtedness.***

As a result of the sale of \$150,000,000 aggregate principal amount of the debentures in May 2003, we increased our total debt and debt service obligations. We may incur substantial additional indebtedness in the future. The level of our indebtedness, among other things, could:

make it difficult for us to make payments on the debentures;

make it difficult for us to obtain any necessary future financing for working capital, capital expenditures, acquisitions or other purposes;

limit our flexibility in planning for, or reacting to changes in, our business; and

make us more vulnerable in the event of a downturn in our business.

There can be no assurance that we will be able to meet our debt service obligations, including our obligations under the debentures.

In addition, we may need to incur debt in the future to fund our business, including any acquisitions we may make, but there can be no assurance that we will be able to incur debt or other financing, on favorable terms or at all, necessary to fund our operations or effect any acquisitions.

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### ***Any adverse rating of the debentures may cause the value of the debentures to fall.***

The debentures have not been rated by any credit rating agencies. In the future, one or more rating agencies may rate the debentures. If the rating agencies rate the debentures, they may assign a lower rating than expected by investors. Rating agencies may also lower ratings on the debentures in the future. If the rating agencies assign a lower than expected rating or reduce their ratings on the debentures in the future or indicate that they have their ratings on the debentures under surveillance or review with possible negative implications, the value of the debentures would likely decline. In addition, a ratings downgrade could adversely affect our ability to access capital.

### ***Absence of market for the debentures.***

We issued the debentures in May 2003 in a private offering made to "qualified institutional buyers," as defined in Rule 144 under the Securities Act. The offering was made through a group of investment banks, which we refer to as the "initial purchasers," for which J.P. Morgan Securities Inc. acted as sole book-running manager. Prior to that offering there was no trading market for the debentures. Although the initial purchasers advised us at the time of that offering that they intended to make a market in the debentures, they are not obligated to do so and may discontinue such market making at any time without notice. Accordingly, there can be no assurance that any market for the debentures will develop or, if one does develop, that it will be maintained. If an active market for the debentures fails to develop or be sustained, the value of the debentures could be materially adversely affected.

There is no public market for the debentures and we do not intend to apply for listing of the debentures on any securities exchange or for quotation of the debentures through any automated quotation system. The debentures issued to qualified institutional buyers in the May 2003

offering currently trade on the PORTAL Market. However, once debentures are sold under this prospectus, those debentures will no longer trade on the PORTAL market.

***You should consider the United States federal income tax consequences of owning the debentures.***

The debentures constitute indebtedness for U.S. federal income tax purposes. Accordingly, you will be required to include, in your income, interest with respect to the debentures.

The debentures constitute contingent payment debt instruments for U.S. federal income tax purposes, and are subject to U.S. federal income tax regulations applicable to contingent payment debt instruments. Under that characterization and treatment, you will be required to include amounts in income, as interest income, in advance of your receipt of the cash or other property attributable to the debentures. The amount of interest income required to be included by you in income for each year, which we refer to as tax original issue discount, generally will be in excess of the accruals on the debentures for non-tax purposes (i.e., in excess of the stated semi-annual regular interest payments and any contingent interest payments) actually received in that year.

You will recognize gain or loss on the sale, purchase by us at your option, exchange, conversion or redemption of a debenture in an amount equal to the difference between the amount realized, including the fair market value of any of our common stock received, and your adjusted tax basis in the debenture. Any gain recognized by you on the sale, purchase by us at your option, exchange, conversion or redemption of a debenture will be treated as ordinary interest income. A discussion of the U.S. federal income tax consequences of ownership of the debentures is contained in this prospectus under the heading "Certain United States federal income tax considerations."

**Cautionary note regarding forward-looking statements and market data**

This prospectus and the documents incorporated or deemed to be incorporated by reference in this prospectus contain "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). We intend the forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these sections. All statements other than statements of historical fact in this prospectus and the documents incorporated or deemed to be incorporated by reference in this prospectus are "forward-looking statements" for purposes of these sections, including, without limitation, any predictions of earnings, revenues, expenses or other financial items, any statements of the plans, strategies and objectives of management for future operations, any statements concerning proposed new products, any statements regarding future economic conditions, any statements concerning our future operations, financial conditions and prospects, and any statement of assumptions underlying any of the foregoing. These statements can sometimes be identified by the use of forward-looking words such as "may," "will," "anticipate," "estimate," "project," "seek," "expect," "continue," "pro forma," "plan" or "intend" or similar words, or expressions of the negative thereof. These forward-looking statements are subject to substantial risks, uncertainties and assumptions. Some of the factors that could cause actual results to differ materially from the forward-looking statements we make or incorporate by reference in this prospectus are described under "Risk factors" in this prospectus and in the documents incorporated or deemed to be incorporated by reference in this prospectus. These factors include, but are not limited to:

our ability to successfully develop, obtain regulatory approvals for and market new products;

our ability to generate and maintain sufficient cash resources to increase investment in our business or repay debt;

the contribution of new product launches;

the impact of currency exchange rates;

the timing or results of pending or future clinical trials;

actions by the U.S. Food and Drug Administration and other regulatory agencies;

technological advances in the medical field;

product demand and market acceptance; and

the effect of changing economic conditions.

If one or more of these risks or uncertainties materialize, or if any underlying assumptions proves incorrect, our actual results, performance or achievements may vary materially from future results, performance or achievements expressed or implied by these forward-looking statements. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements in this section. We undertake no obligation to update or revise any forward-looking statements to reflect future events or developments.

The information in this prospectus and the documents incorporated or deemed to be incorporated by reference in this prospectus includes statements concerning our position in certain markets and other demographic, statistical and similar information. These statements, which reflect the belief of our management based upon the sources of information described below, include statements that we are a leader or the leader or a leading or the leading company or manufacturer in some of our markets or globally or with respect to some of our products, systems, therapies or technologies, that one of our heart valve products is more widely prescribed than other heart valves worldwide, regarding the number of patients using some of our products, regarding the number of patients affected by certain diseases or

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that use certain of our products, regarding whether patients undergoing surgical treatment for cardiovascular disease are likely to encounter our products and technologies or are candidates to have their cardiac function monitored by our products, regarding the factors that cause certain diseases, regarding the absence of reportings of "mad cow" disease cases in the United States, regarding the risk of infectibility of tissue types used in our pericardial tissue valve products, regarding the number of deaths caused by cardiovascular disease and its ranking compared to other diseases in terms of healthcare spending, regarding the increasing number of "beating heart" coronary artery bypass surgeries, that one of our products is the only pericardial valve available in the U.S., that certain of our products are widely-known or recognized as an or the industry standard, regarding the level of the engagement of our workforce, that we are a pioneer of certain products, regarding market share data, regarding the medical device industry, the healthcare industry and the cardiovascular products market, and similar matters.

The information reflected in the statements described above is based on, among other things, publicly available information, industry publications, data compiled by market research firms and similar sources. Although we believe that this information is reliable, we have not independently verified any of this information and we cannot assure you that it is accurate. In addition, most of this information relates to years or periods prior to 2002. Statements that we are a leader or the leader, or that we are a leading or the leading company or manufacturer in some of our markets or globally or with respect to some of our products, systems, therapies or technologies, are generally based on our net sales or units sold. The statement that cardiovascular disease is among the top three diseases in terms of healthcare spending that is incorporated by reference into this prospectus is based on data for the U.S.

#### **Use of proceeds**

We will not receive any of the proceeds from the sale by any selling securityholders of debentures or the common stock issued upon conversion of the debentures.

#### **Dividend policy**

We have never paid any dividends on our common stock and have no current plans to pay any dividends on our common stock. Our current policy is to retain any future earnings for use in our business.

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**Ratio of earnings to fixed charges**

The following table presents the ratio of earnings to fixed charges for Edwards Lifesciences Corporation and its consolidated subsidiaries for each of the periods indicated. Edwards Lifesciences was incorporated on September 10, 1999 as a wholly owned subsidiary of Baxter International Inc. to assume the business and operations of Baxter's CardioVascular Group. Effective March 31, 2000, the business, assets and liabilities of Baxter's CardioVascular Group were transferred to us and our subsidiaries and 100% of our common stock was distributed to the stockholders of Baxter in a tax-free spin-off (the "Distribution"). As a result, the following information for periods prior to April 1, 2000 presents Edwards Lifesciences on a divisional basis as we had historically been operated as a part of Baxter, and has been prepared using Baxter's historical bases in the assets and liabilities and the historical results of operations of Baxter's CardioVascular Group prior to the Distribution. The following information does not necessarily reflect what our ratio of earnings to fixed charges would have been had we operated as a stand-alone entity during the periods prior to the Distribution.

	Years ended December 31,					Three months ended March 31, 2003
	1998	1999	2000	2001	2002	
Ratio of earnings to fixed charges(1)	(2)	(2)	(3)	(3)	5.7x	8.9x

- (1) The ratio of earnings to fixed charges is unaudited for all periods presented. For the purpose of calculating the ratio of earnings to fixed charges, earnings consist of net income (loss) plus the provision for income taxes and fixed charges, and excludes the cumulative effect of a change in accounting principle. Fixed charges consist of interest expense, amortization of debt issuance costs and the estimated portion of rental expenses deemed to be equivalent to interest.
- (2) Until March 31, 2000 (the date of the Distribution), we were operated as a division of Baxter and our business and operations were therefore funded with monies provided by Baxter.
- (3) For the years ended December 31, 2000 and 2001, fixed charges exceeded earnings by \$258.4 million and \$8.4 million, respectively.

**Description of the debentures**

The debentures were issued under an indenture dated as of May 9, 2003 between us and JPMorgan Chase Bank, as trustee. The following summary of certain provisions of the indenture and the debentures does not purport to be complete, and is subject to, and is qualified in its entirety by reference to, all of the provisions of the debentures and the indenture. Because the following is only a summary, it does not contain all information that you may find useful. Copies of the indenture and the form of debenture have been filed or incorporated by reference as exhibits to the registration statement of which this prospectus is a part and you may obtain copies of those documents as described below under "Available information" and "Incorporation of documents by reference."

As used in this "Description of the debentures," unless otherwise expressly stated or the context otherwise requires, the words "Edwards Lifesciences," "we," "our" and "us" refer to Edwards Lifesciences Corporation, excluding its subsidiaries.

**General**

The debentures are our unsecured and unsubordinated obligations and were issued in, and are limited to, an aggregate principal amount of \$150,000,000. The debentures will mature on May 15, 2033, unless earlier converted, redeemed by us at our option or repurchased by us at the option of the holders. The debentures are issuable only in fully registered form without coupons in denominations of \$1,000 and integral multiples of \$1,000 principal amount.

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You have the option, subject to certain conditions described below, to convert your debentures into shares of our common stock, initially at a conversion price of \$54.66 per share of common stock. This is equivalent to an initial conversion rate of approximately 18.2949 shares of common stock per \$1,000 principal amount of debentures. The conversion price is subject to adjustment from time to time if certain events described below occur. Upon conversion, you will receive only shares of our common stock and a cash payment in lieu of any fractional shares. You will not receive any cash payment for interest or contingent interest, if any, accrue

- (i) reviewing, modifying and approving our overall compensation strategy and policies;
- (ii) reviewing and approving corporate and individual performance goals relevant to the compensation of our executive officers;
- (iii) evaluating and recommending to our Board of Directors compensation plans and programs for us, as well as modifying or terminating existing plans and programs;
- (iv) reviewing and approving compensation and benefits for our non-employee directors and executive officers, and making recommendations to our Board of Directors regarding these matters;
- (v) authorizing and approving equity grants under our equity compensation plans; and
- (vi) overseeing preparation and review of the committee's report and the compensation discussion and analysis included in our proxy statement.

Our Board of Directors has adopted a written charter for the Compensation Committee, which is available on our website at [www.arenapharm.com](http://www.arenapharm.com). Mr. Belcher is the Chair of the Compensation Committee. The Compensation Committee held five meetings in 2008. The Compensation Committee's report is set forth below under Compensation Committee Report.

### ***Corporate Governance and Nominating Committee***

The Corporate Governance and Nominating Committee's responsibilities include:

- (i) recommending guidelines to our Board of Directors for our corporate governance, including the structure and function of our Board and its committees and our management;
- (ii) reviewing and approving a management succession plan and related procedures;
- (iii) making recommendations regarding the agenda for our Board of Directors' strategy discussions;
- (iv) overseeing compliance related policies and practices that are not within the purview of the Audit Committee or are referred by our Board of Directors;
- (v) establishing criteria for membership on our Board of Directors;
- (vi) identifying, evaluating, reviewing and recommending to our Board of Directors qualified candidates to serve on our Board;
- (vii) making recommendations to our Board of Directors regarding the election of officers;



- (viii) serving as a focal point for communications between director candidates, non-committee directors and management; and
- (ix) reviewing and assessing the performance of our Board of Directors and each of its committees.

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The Corporate Governance and Nominating Committee uses many sources to identify potential director candidates, including the network of contacts among our directors, officers and other employees, and may engage outside consultants and recruiters in this process. As set forth below under Stockholder Director Recommendations, the Corporate Governance and Nominating Committee will consider director candidates recommended by our stockholders. The Corporate Governance and Nominating Committee believes that candidates for director should have certain minimum qualifications, including being able to understand basic financial statements. In considering candidates for director, the Corporate Governance and Nominating Committee will consider all relevant factors, which may include, among others, the candidate's experience and accomplishments, the relevance of such experience to our business, the availability of the candidate to devote sufficient time and attention to our company, the candidate's reputation for integrity and ethics and the candidate's ability to exercise sound business judgment. The Corporate Governance and Nominating Committee retains the right to modify these qualifications from time to time, and candidates for director are reviewed in the context of the composition of the then current Board of Directors, our requirements and the interests of our stockholders. The Corporate Governance and Nominating Committee recommended the nominations of each of the directors nominated for election at our 2009 Annual Meeting.

Our Board of Directors has adopted a written charter for the Corporate Governance and Nominating Committee, which is available on our website at [www.arenapharm.com](http://www.arenapharm.com). Dr. White is the Chair of the Corporate Governance and Nominating Committee. The Corporate Governance and Nominating Committee held three meetings in 2008.

### **Stockholder Director Recommendations**

The Corporate Governance and Nominating Committee will consider director candidates recommended by our stockholders. A candidate must be highly qualified and be willing and expressly interested in serving on our Board of Directors. To be considered by the Corporate Governance and Nominating Committee, a stockholder recommendation for director candidates for an annual meeting of stockholders must be received by the committee by December 31 of the year before such annual meeting. A stockholder who wishes to recommend a candidate for the Corporate Governance and Nominating Committee's consideration should forward the candidate's name and information about the candidate's qualifications to Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121. **Submissions must include a representation that the nominating stockholder is a beneficial or record owner of our stock. Any such submission must be accompanied by the written consent of the proposed nominee to be named as a nominee and to serve as a director if elected.** This procedure does not affect the deadline for submitting other stockholder proposals for inclusion in the proxy statement, nor does it apply to questions a stockholder may wish to ask at an annual meeting. Additional information regarding submitting stockholder proposals is set forth in our Bylaws. Stockholders may request a copy of the bylaw provisions relating to stockholder proposals from our Corporate Secretary.

### **Stockholder Communications with our Board of Directors**

Our Board of Directors has a formal process by which stockholders may communicate with our Board or any of our directors or officers. Stockholders who wish to communicate with our Board of Directors or any of our directors or officers may do so by sending written communications addressed to such person or persons in care of Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121. All such communications to our directors will be compiled by our Corporate Secretary and submitted to the addressees on a periodic basis. If our Board of Directors modifies this process, we will post the revised process on our website.

### **Compensation Committee Interlocks and Insider Participation**

Messrs. Belcher and Bice and Drs. Hixson, La Force and White served on the Compensation Committee for at least part of 2008, and the committee currently consists of Messrs. Belcher and Bice and Drs. Hixson and

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White. No director serving on the Compensation Committee during any part of 2008 was, at any time during or before such fiscal year, one of our employees. None of our executive officers served during any part of 2008 as a member of the board of directors or compensation committee of any other entity that had one or more of its executive officers serving as members of our Board of Directors or its Compensation Committee.

### **Certain Relationships and Related Transactions**

Except for the compensation arrangements between us and our executive officers and directors described below under Compensation Discussion and Analysis, since January 1, 2008, we have not been a party to any transactions involving more than \$120,000 and in which any director, nominee for director, executive officer, holder of more than 5% of our common stock or any immediate family member of the foregoing has a direct or indirect material interest, nor are any such transactions currently proposed.

The Audit Committee's charter requires that it reviews and approves any related-party transactions. In considering related-party transactions, the Audit Committee considers the relevant available facts and circumstances, including, but not limited to, (i) the risks, costs and benefits to us, (ii) the impact on a director's independence in the event the related party is a director, immediate family member of a director or an entity with which a director is affiliated, (iii) the terms of the transaction, (iv) the availability of other sources for comparable services or products, and (v) the terms available to or from, as the case may be, unrelated third parties or to or from employees generally. In the event a director has an interest in the proposed transaction, the director must recuse himself or herself from the deliberations and approval. In determining whether to approve, ratify or reject a related-party transaction, the Audit Committee evaluates whether, in light of known circumstances, the transaction is in, or is not inconsistent with, our best interests and those of our stockholders.

#### **Approval of the Arena Pharmaceuticals, Inc., 2009 Long-Term Incentive Plan (*Proposal 2*)**

Stockholders are being asked to approve the Arena Pharmaceuticals, Inc., 2009 Long-Term Incentive Plan (the 2009 LTIP). The Board of Directors approved the 2009 LTIP at its April 17, 2009 meeting, subject to approval from stockholders at the 2009 Annual Meeting. The Board of Directors considers the 2009 LTIP to be a significant contributor to our long-term financial success, by assisting us in attracting and retaining individuals who are expected to contribute to our success by serving as employees, directors, consultants and/or advisors and to assist us in achieving long-term objectives that we believe will benefit our stockholders.

When we adopted our 2006 Long-Term Incentive Plan, as amended (the 2006 LTIP), in June 2006, our Amended and Restated 1998 Equity Compensation Plan, Amended and Restated 2000 Equity Compensation Plan, and 2002 Equity Compensation Plan were terminated (together with the 2006 LTIP, the Prior Plans). Subject to and upon approval of the 2009 LTIP by stockholders at the 2009 Annual Meeting, our 2006 LTIP will also be terminated. However, notwithstanding such termination of the Prior Plans, all outstanding awards under the Prior Plans will continue to be governed under the terms of the Prior Plans.

There will be 7.0 million shares of our common stock authorized for issuance under the 2009 LTIP if it is approved by stockholders, which amount will be (i) decreased for grants made since December 31, 2008 and before the approval of the 2009 LTIP and (ii) increased by the number of shares subject to any stock awards under the Prior Plans that, after December 31, 2008, are forfeited, expire or settled for cash and as otherwise provided in the 2009 LTIP.

The following summary describes the principal features of the 2009 LTIP, and is qualified in its entirety by reference to the full text of the 2009 LTIP. A copy of the 2009 LTIP is filed as Appendix A to the proxy statement for the 2009 Annual Meeting filed with the SEC.

In this Proposal 2, stockholders are requested to approve the adoption of the 2009 LTIP. The affirmative vote of the holders of a majority of the shares of common stock present in person or represented by proxy and

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entitled to vote at the 2009 Annual Meeting will be required to approve the adoption of the 2009 LTIP. Abstentions will be counted toward the tabulation of votes cast on proposals presented to the stockholders and will have the same effect as negative votes. Broker non-votes are counted towards a quorum, but are not counted for any purpose in determining whether this matter has been approved.

**Summary of the 2009 Long-Term Incentive Plan**

*Purpose.* The purpose of the 2009 LTIP is to assist us in attracting and retaining selected individuals who, serving as our employees, directors, consultants and/or advisors, are expected to contribute to our success and achieve long-term objectives that will inure to the benefit of all of our stockholders through the additional incentives inherent in the awards under the 2009 LTIP.

*Shares Available for Issuance.* Up to 7.0 million shares of common stock will be available for issuance under the 2009 LTIP, subject to adjustment for certain corporate events, including mergers and stock splits. This amount consists of 5.8 million shares of common stock, plus the number of unallocated shares remaining in the 2006 LTIP on December 31, 2008. Stock options and stock appreciation rights granted under the Prior Plans after December 31, 2008 or under the 2009 LTIP reduce the available number of shares by 1 share for every share issued while awards other than stock options and stock appreciation rights granted under the Prior Plans after December 31, 2008 or under the 2009 LTIP reduce the available number of shares by 1.3 shares for every share issued. In addition, shares that, after December 31, 2008, are released from awards granted under the Prior Plans because the awards expire, are forfeited or are settled for cash will increase the number of shares available under the 2009 LTIP by 1 share for each share released from a stock option or stock appreciation right and by 1.3 shares for each share released from a restricted stock award or restricted stock unit award. The following shares will not become available for issuance: (i) shares tendered or withheld in payment of the purchase price of an option, or to satisfy any tax withholding obligation with respect to an option or stock appreciation right, (ii) shares subject to a stock appreciation right that are not issued in connection with the stock settlement of the stock appreciation right on exercise thereof, and (iii) shares reacquired on the open market or otherwise using cash proceeds from the exercise of options or options granted under the Prior Plans. Shares issued under awards granted in assumption of or in substitution for awards previously granted by a company acquired by us or with which we or any subsidiary combines, will not reduce the shares authorized for issuance under the 2009 LTIP. Shares issued under the 2009 LTIP may consist of authorized and unissued shares, treasury shares or shares purchased in the open market or otherwise.

*Eligibility; Awards to be Granted to Certain Individuals and Groups.* Options, stock appreciation rights, restricted stock awards, restricted stock unit awards and performance awards may be granted under the 2009 LTIP. Options may be either incentive stock options, as defined in Section 422 of the Internal Revenue Code of 1986, as amended (the Code), or nonstatutory stock options. Awards may be granted under the 2009 LTIP to any employee, non-employee member of the Board of Directors, consultant or advisor who provides us service, except for incentive stock options which may be granted only to our employees or employees of our subsidiaries.

As of April 24, 2009, approximately 500 employees and eight non-employee directors were eligible to participate in the 2009 LTIP. These employees include (i) our six executive officers, (ii) approximately 70 employees at our Swiss subsidiary, Arena Pharmaceuticals GmbH, and (iii) approximately 130 employees selected for a reduction in force that is expected to be substantially completed by June 22, 2009. The Compensation Committee, in its discretion, selects the individual or individuals to whom awards under the 2009 LTIP may be granted, determines the type or types of awards to be granted, the time or times at which such awards shall be granted, and the number of shares subject to each such grant (or the dollar value of certain performance awards). For this reason, it is not possible to determine the benefits or amounts that will be received by any particular individual or individuals in the future.

*Certain Limits on Shares Subject to Awards.* The 2009 LTIP provides that no participant may be granted, in any 36-month period, (i) options or stock appreciation rights to purchase more than 2.0 million shares of

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common stock, or (ii) restricted stock awards, performance awards and/or restricted stock unit awards that are denominated in shares with respect to more than 1.0 million shares of common stock that are intended to comply with the performance-based exception under Code Section 162(m). Shares subject to a cancelled award continue to count against the applicable limit. The maximum dollar value that may be granted to any participant for each 12 months in a performance period with respect to performance-based awards that are intended to comply with the performance-based exception under Code Section 162(m) and are denominated in cash is \$5,000,000. The dollar value of a cancelled award will continue to count against the \$5,000,000 limit.

The aggregate maximum number of shares of common stock that may be issued under the 2009 LTIP pursuant to the exercise of incentive stock options is 7.0 million shares, subject to adjustment for certain corporate events, including mergers and stock splits.

*Administration.* The Plan will be administered by the Compensation Committee, which shall consist of at least two directors, both of whom must qualify as non-employee directors under Rule 16b-3 under the Exchange Act, outside directors under Section 162(m) of the Code and independent directors for purposes of the rules of the NASDAQ Stock Market to the extent required by such rules. The Compensation Committee has the authority to select the participants who will receive awards under the 2009 LTIP, to determine the type and terms of the awards, and to interpret and administer the 2009 LTIP. The Compensation Committee may delegate the right to make grants and otherwise take action on the Compensation Committee's behalf under the 2009 LTIP to a committee of one or more directors and, to the extent permitted by law, to an executive officer or a committee of executive officers the right to grant awards to employees who are not our executive officers.

*Terms and Conditions of Options.* Options granted under the 2009 LTIP may be incentive stock options, nonstatutory stock options, or a combination thereof, and are subject to the following terms and conditions:

*Exercise Price.* The exercise price of options granted under the 2009 LTIP is determined by the Compensation Committee at the time the options are granted. The exercise price of an option may not be less than 100% of the fair market value of the common stock on the date such option is granted, except in the case of substitute awards granted in connection with an acquisition; provided, however, that in the case of an incentive stock option granted to a participant who, at the time of the grant, owns stock representing more than 10% of the voting power of all of our classes of stock, the option price per share will be no less than 110% of the fair market value of one share of our common stock on the date of grant. The fair market value of the common stock is generally determined with reference to the closing price for the common stock on the NASDAQ Stock Market on the date the option is granted (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported). On April 24, 2009, the closing price of our common stock as reported on the NASDAQ Stock Market was \$2.46 per share.

*Exercise of Option.* The Compensation Committee determines when options become exercisable. The 2009 LTIP permits payment to be made by cash, check, other shares of our common stock, any other form of consideration approved by the Compensation Committee (including withholding of shares of common stock that would otherwise be issued on exercise of options) and permitted by applicable law, or any combination thereof.

*Term of Option.* Options granted under the 2009 LTIP expire no later than 10 years from the date of grant, except in the event of the optionee's death or disability; provided, however, that the term of the option will not exceed five years from the date the option is granted in the case of an incentive stock option granted to a participant who, at the time of the grant, owns stock representing more than 10% of the voting power of all of our classes of stock.

*Stock Appreciation Rights.* The Compensation Committee is authorized to grant stock appreciation rights in conjunction with an option or other award granted under the 2009 LTIP, and to grant stock appreciation rights separately. The grant price of a stock appreciation right may not be less than 100% of the fair market value of the common stock on the date such stock appreciation right is granted, except in the case of substitute awards

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granted in connection with an acquisition. The Compensation Committee determines when stock appreciation rights become exercisable. The term of a stock appreciation right may be no more than 10 years from the date of grant.

Upon the exercise of a stock appreciation right, the holder will have the right to receive the excess of the fair market value of the shares or, at the discretion of the Compensation Committee, such lesser amount, on the date of exercise over the grant price. Payment may be made in cash, shares of our common stock or other property, or any combination of the same, as the Compensation Committee may determine. Shares issued upon the exercise of a stock appreciation right are valued at their fair market value as of the date of exercise.

*Restricted Stock Awards.* Restricted stock awards may be issued to participants either alone or in addition to other awards granted under the 2009 LTIP, and are also available as a form of payment for performance awards and other earned cash-based incentive compensation. The Compensation Committee determines the terms and conditions of restricted stock awards, including the number of shares granted (subject to the limit on shares subject to awards set forth above), and any conditions for vesting that must be satisfied, which typically will be based principally or solely on continued provision of services, but may include a performance-based component.

*Restricted Stock Unit Awards.* Awards of restricted stock units having a value equal to an identical number of shares may be granted either alone or in addition to other awards granted under the 2009 LTIP, and are also available as a form of payment for other awards granted under the 2009 LTIP and other earned cash-based incentive compensation. Restricted stock units may be paid in cash, shares of common stock or other property, or a combination thereof, as determined by the Compensation Committee. The Compensation Committee determines the other terms and conditions of restricted stock units.

*Performance Awards.* Performance awards provide participants with the opportunity to receive cash, shares of common stock or other property, or any combination thereof, based on performance and other vesting conditions. Performance awards may be granted from time to time as determined at the discretion of the Compensation Committee. Subject to the share limit and maximum dollar value set forth above, the Compensation Committee has the discretion to determine (i) the number of shares of common stock under, or the dollar value of, a performance award and (ii) the conditions that must be satisfied for grant or for vesting, which typically will be based principally or solely on achievement of performance goals. The minimum performance period under a performance award is 12 months.

If this Proposal 2 is approved by the stockholders, compensation attributable to performance awards under the 2009 LTIP will qualify as performance-based compensation under Section 162(m) of the Code, provided that: (i) the compensation is granted by a compensation committee comprised solely of outside directors, (ii) the compensation is paid only upon the achievement of an objective performance goal established in writing by the Compensation Committee while the outcome is substantially uncertain, and (iii) the Compensation Committee certifies in writing prior to the payment of the compensation that the performance goal has been satisfied.

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*Code Section 162(m) Performance Awards.* The 2009 LTIP is designed to permit us to issue awards that qualify as performance-based under Section 162(m) of the Code, by making performance goals meeting the requirements of Section 162(m) applicable to a participant with respect to an award. At the Compensation Committee's discretion, performance goals shall be based on the attainment of specified levels of one or any combination of the following:

net sales;	gross margin;	strategic partnerships or transactions (including in-licensing and out-licensing of intellectual property);
revenue;	year-end cash;	
revenue or product revenue growth;	cash margin;	establishing relationships with commercial entities with respect to the marketing, distribution and sale of our products (including with group purchasing organizations, distributors and other vendors);
operating income or loss (before or after taxes);	debt reduction;	
pre- or after-tax income or loss (before or after allocation of corporate overhead and bonus);	stockholder's equity;	
net earnings or loss;	market share;	
earnings or loss per share;	achievement of drug development milestones;	supply chain achievements (including establishing relationships with manufacturers or suppliers of active pharmaceutical ingredients and other component materials and manufacturers of our products);
net income or loss (before or after taxes);	regulatory achievements including approval of a compound;	
return on equity;	progress of internal research or clinical programs;	
total stockholder return;	progress of partnered programs;	co-development, co-marketing, profit sharing, joint venture or other similar arrangements;
return on assets or net assets;		

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attainment of strategic and operational initiatives;	implementation or completion of projects and processes;	financing and other capital raising transactions (including sales of our equity or debt securities);
appreciation in and/or maintenance of the price of our stock;	partner satisfaction;	factoring transactions;
market share;	budget management;	sales or licenses of our assets, including intellectual property (whether in a particular jurisdiction or territory or globally or through partnering transactions);
gross profits;	clinical achievements;	
earnings or losses (including earnings or losses before taxes, earnings or losses before interest and taxes, earnings or losses before interest, taxes and depreciation or earnings or losses before interest, taxes, depreciation and amortization);	completing phases of a clinical study (including the treatment phase); or announcing or presenting preliminary or final data from clinical studies; in each case, whether on particular timelines or generally);	
economic value-added models (or equivalent metrics);	timely completion of clinical trials;	implementation, completion or attainment of measurable objectives with respect to research, development, manufacturing, commercialization, products or projects, production volume levels, acquisitions and divestitures;
comparisons with various stock market indices;	submission of INDs and NDAs and other regulatory achievements;	
reductions in costs;	partner or collaborator achievements;	
cash flow or cash flow per share (before or after dividends);	internal controls, including those related to the Sarbanes-Oxley Act of 2002;	factoring transactions; and
return on capital (including return on total capital or return on invested capital);	research progress, including the development of programs;	recruiting and maintaining personnel.
cash flow return on investment;	financing;	
	investor relation, analysts and communication;	



improvement in or attainment of expense levels or working capital levels;

manufacturing achievements (including obtaining particular yields from manufacturing runs and other measurable objectives related to process development activities);

operating margin;

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Such performance goals also may be based solely by reference to our performance or the performance of one or more of our affiliates, divisions, business segments or business units, or based upon the relative performance of other companies or upon comparisons of any of the indicators of performance relative to other companies. At the time a performance award is granted, the Compensation Committee may also exclude charges related to an event or occurrence which the Compensation Committee determines should appropriately be excluded, including (i) restructurings, discontinued operations, extraordinary items, and other unusual or non-recurring charges, (ii) an event either not directly related to our operations or not within the reasonable control of our management, or (iii) the cumulative effects of tax or accounting changes in accordance with US generally accepted accounting principles.

*Dividends; Dividend Equivalents.* Awards other than options and stock appreciation rights may, if so determined by the Compensation Committee, provide that the participant will be entitled to receive cash, or stock or other property dividends, or cash payments in amounts equivalent to cash, stock or other property dividends declared with respect to shares of common stock covered by an award. The Compensation Committee may provide that such amounts shall be deemed to have been reinvested in additional shares of common stock or otherwise, and that they are subject to the same vesting or performance conditions as the underlying award.

*Termination of Service.* The Compensation Committee will determine and set forth in each award agreement whether an award will continue to be exercisable, continue to vest or be earned and the terms of such exercise, vesting or earning, on and after the date that a participant terminates employment or service with us, whether by reason of death, disability, voluntary or involuntary termination of employment or services, or otherwise.

*No Repricing.* The 2009 LTIP prohibits option and stock appreciation right repricings (other than to reflect stock splits, spin-offs or other corporate events described under *Adjustments upon Changes in Capitalization* below) unless stockholder approval is obtained. For purposes of the 2009 LTIP, a repricing means a reduction in the exercise price of an option or the grant price of a stock appreciation right, the cancellation of an option or stock appreciation right in exchange for cash or another award (except for awards granted in assumption of or in substitution for awards previously granted by a company acquired by us or with which we combine) under the 2009 LTIP if the exercise price of the cancelled option or grant price of the cancelled stock appreciation right is greater than the fair market value of the common stock, or any other action with respect to an option or stock appreciation right that may be treated as a repricing under the NASDAQ marketplace rules.

*Nontransferability of Awards.* Except as provided in the next sentence, an award granted under the 2009 LTIP is not transferable other than by will or the laws of descent and distribution, and may be exercised during the participant's lifetime only by the participant or the participant's guardian or legal representative. The Compensation Committee may provide in an award agreement that a participant may transfer an award (other than an incentive stock option) to a family member (whether by gift or a domestic relations order) under such terms and conditions determined by the Compensation Committee.

*Adjustments upon Changes in Capitalization.* In the event of any merger, reorganization, consolidation, recapitalization, dividend or distribution (whether in cash, shares or other property, other than a regular cash dividend), stock split, reverse stock split, spin-off or similar transaction or other change in our corporate structure affecting our common stock or the value thereof, appropriate adjustments shall be made, in the discretion of the Compensation Committee, in the number and class of shares of stock subject to the 2009 LTIP, the number and class of shares of awards outstanding under the 2009 LTIP, the limits on the number of awards that any person may receive and the exercise price of any outstanding option or stock appreciation right.

*Change in Control.* The Compensation Committee may, in its discretion, determine that, upon our *Change in Control* (as that term is defined in the 2009 LTIP or otherwise defined in the agreement evidencing an award), options and stock appreciation rights outstanding as of the date of the *Change in Control* shall be cancelled and terminated without payment therefor if the fair market value of one share of our common stock as of the date of the *Change in Control* is less than the per share option exercise price or stock appreciation right grant price.

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To the extent provided in an award agreement, in the event of a Change in Control in which the successor company assumes or substitutes for an option, stock appreciation right, restricted stock award or restricted stock unit award (or in which we are the ultimate parent corporation and continue the award), if a participant's employment with such successor company (or us) or a subsidiary thereof within the period following such Change in Control set forth in the award agreement (or prior if applicable) under the circumstances set forth in the award agreement, each award held by such participant at the time of such termination of employment will be fully vested, and options and stock appreciation rights may be exercised during the period following such termination set forth in the award agreement. If the successor company does not assume or substitute for such outstanding awards held by participants at the time of the Change in Control, then unless otherwise provided in the award agreement, the awards will become fully vested immediately prior to the Change in Control and will terminate immediately after the Change in Control.

The Compensation Committee, in its discretion, may also determine that, upon the occurrence of a Change in Control, each option and stock appreciation right outstanding shall terminate within a specified number of days after notice to the participant, and/or that each participant shall receive, with respect to each share of common stock subject to such option or stock appreciation right, an amount equal to the excess, if any, of the fair market value of such share immediately prior to the occurrence of such Change in Control over the exercise price per share of such option and/or stock appreciation right; such amount to be payable in cash, in one or more kinds of stock or property, or in a combination thereof, as the Compensation Committee, in its discretion, will determine.

*Effective Date.* The 2009 LTIP will be effective upon its approval by stockholders at the 2009 Annual Meeting.

*Amendment and Termination of the 2009 LTIP.* The Board of Directors may alter, amend, suspend or terminate the 2009 LTIP, from time to time as it deems advisable, subject to any requirement of applicable law or the rules and regulations of the NASDAQ Stock Market for stockholder approval. However, the Board of Directors may not amend the Plan without stockholder approval to increase the number of shares available for awards under the 2009 LTIP, expand the types of awards available under the 2009 LTIP, materially expand the class of persons eligible to participate in the 2009 LTIP, permit the grant of options or stock appreciation rights with an exercise or grant price of less than 100% of fair market value on the date of grant (except for substitute awards granted in connection with an acquisition), increase the maximum term of options and stock appreciation rights, increase the limits on shares subject to awards or the dollar value payable with respect to performance awards, or take any action with respect to an option that may be treated as a repricing under the NASDAQ marketplace rules and related guidance. No such action by the Board of Directors may alter or impair any award previously granted under the 2009 LTIP without the written consent of the participant. The 2009 LTIP will expire on the 10th anniversary of its effective date, except with respect to awards then outstanding, and no further awards may be granted thereafter.

*US Federal Income Tax Consequences.* The following discussion summarizes certain federal income tax considerations of awards under the 2009 LTIP. However, it does not purport to be complete and does not describe the state, local or foreign tax considerations or the consequences for any particular individual.

*Incentive Stock Options.* An optionee who is granted an incentive stock option does not recognize taxable income at the time the option is granted or upon its exercise, although the exercise may subject the optionee to the alternative minimum tax. Upon an optionee's sale of the shares (assuming that the sale occurs more than two years after grant of the option and more than one year after exercise of the option), any gain will be taxed to the optionee as long-term capital gain. If the optionee disposes of the shares prior to the expiration of the above holding periods, then the optionee will recognize ordinary income in an amount generally measured as the excess, if any, of the fair market value of the shares at the exercise date or the sale price of the shares, whichever is lower, over the exercise price. Any gain or loss recognized on such sale of the shares in excess of the amount treated as ordinary income will be characterized as long-term or short-term capital gain or loss, depending on the holding period.

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*Nonstatutory Stock Options.* An optionee does not recognize any taxable income at the time a nonstatutory stock option is granted. Upon exercise, the optionee recognizes taxable ordinary income measured by the excess of the fair market value of the shares on the exercise date over the exercise price. Upon a disposition of such shares by the optionee, any difference between the amount recognized on the sale and the fair market value of the shares on the exercise date is treated as long-term or short-term capital gain or loss, depending on the holding period.

*Stock Appreciation Rights.* No income will be recognized by a recipient in connection with the grant of a stock appreciation right. When the stock appreciation right is exercised, the recipient will recognize ordinary income in the year of exercise in an amount equal to the sum of the amount of any cash received and the fair market value of any common stock or other property received upon the exercise.

### *Restricted Stock Awards and Performance Awards*

Generally, the recipient of a restricted stock award or a performance award will recognize ordinary compensation income at the time the stock is received equal to the excess, if any, of the fair market value of the stock received over any amount paid by the recipient in exchange for the stock. If, however, the stock is not vested when it is received (for example, if the employee is required to work for a period of time to have the right to sell the stock), the recipient generally will not recognize income until the stock becomes vested, at which time the recipient will recognize ordinary compensation income equal to the excess, if any, of the fair market value of the stock on the date it becomes vested over any amount paid by the recipient in exchange for the stock. A recipient may, however, file an election with the Internal Revenue Service, within 30 days of his or her receipt of the stock award, to recognize ordinary compensation income, as of the date the recipient receives the award, equal to the excess, if any, of the fair market value of the stock on the date the award is granted over any amount paid by the recipient in exchange for the stock.

The recipient's basis for the determination of gain or loss upon the subsequent disposition of shares acquired from stock awards will be the amount paid for such shares plus any ordinary income recognized either when the stock is received or when the stock becomes vested.

### *Restricted Stock Units*

Generally, the recipient of a stock unit structured to conform to the requirements of Section 409A of the Code or an exception to Section 409A of the Code will recognize ordinary compensation income at the time the stock is delivered equal to the excess, if any, of the fair market value of the shares of our common stock received over any amount paid by the recipient in exchange for the shares of our common stock. To conform to the requirements of Section 409A of the Code, the shares of our common stock subject to a stock unit award may generally only be delivered upon one of the following events: a fixed calendar date (or dates), separation from service, death, disability or a change in control. If delivery occurs on another date, unless the stock units otherwise comply with or qualify for an exception to the requirements of Section 409A of the Code, in addition to the tax treatment described above, the recipient will owe an additional 20% federal tax and interest on any taxes owed.

The recipient's basis for the determination of gain or loss upon the subsequent disposition of shares acquired from stock units, will be the amount paid for such shares plus any ordinary income recognized when the stock is delivered.

*Company Tax Deduction.* We generally will be entitled to a tax deduction in connection with an award under the 2009 LTIP (subject to the requirement of reasonableness, the provisions of Section 162(m) of the Code and the satisfaction of a tax reporting obligation) in an amount equal to the ordinary income recognized by a participant and at the time the participant recognizes such income (for example, on the exercise of a nonqualified stock option). Section 162(m) of the Code may limit the deductibility of compensation paid to the chief executive officer and to each of the three most highly compensated executive officers other than the chief executive officer and the chief financial officer. Under Section 162(m), the annual compensation paid to any of these specified

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executives will be deductible only to the extent that it does not exceed \$1,000,000. However, we can preserve the deductibility of certain compensation in excess of \$1,000,000 if the conditions of Section 162(m) are met with respect to awards.

Certain kinds of compensation, including qualified performance-based compensation, are disregarded for purposes of the deduction limitation. In accordance with Treasury Regulations issued under Section 162(m) of the Code, compensation attributable to stock options and stock appreciation rights will qualify as performance-based compensation if such awards are approved by a compensation committee comprised solely of outside directors and the plan contains a per-employee limitation on the number of shares for which such awards may be granted during a specified period, the per-employee limitation is approved by the stockholders, and the exercise or strike price of the award is no less than the fair market value of the stock on the date of grant.

Compensation attributable to restricted stock awards, restricted stock unit awards and performance awards will qualify as performance-based compensation, provided that: (i) the compensation is approved by a compensation committee comprised solely of outside directors, (ii) the compensation is paid only upon the achievement of an objective performance goal established in writing by the Compensation Committee while the outcome is substantially uncertain, (iii) the Compensation Committee certifies in writing prior to the payment of the compensation that the performance goal has been satisfied, and (iv) prior to the payment of the compensation, stockholders have approved the material terms of the award (including the class of employees eligible for such award, the business criteria on which the performance goal is based, and the maximum amount, or formula used to calculate the amount, payable upon attainment of the performance goal).

The 2009 LTIP has been designed to permit the Compensation Committee to grant certain awards that qualify as performance-based for purposes of satisfying the conditions of Section 162(m), thereby permitting us to receive a full federal income tax deduction in connection with such awards.

***THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE APPROVAL OF THE 2009 LONG-TERM INCENTIVE PLAN.***

**Approval of the Arena Pharmaceuticals, Inc., 2009 Employee Stock Purchase Plan (Proposal 3)**

Stockholders are being asked to approve the Arena Pharmaceuticals, Inc., 2009 Employee Stock Purchase Plan (the 2009 ESPP). The Board of Directors approved the 2009 ESPP at its April 17, 2009 meeting, subject to approval from stockholders at the 2009 Annual Meeting. The 2009 ESPP is intended to encourage employee participation in the ownership of the company by offering employees the opportunity to purchase our common stock through accumulated payroll deductions.

Our 2001 Employee Stock Purchase Plan, as amended (the 2001 ESPP) will be terminated, subject to and upon approval of the 2009 ESPP by stockholders at the 2009 Annual Meeting. However, notwithstanding such termination of the 2001 ESPP, all Offering Periods existing under the 2001 ESPP on the effective date of the 2009 ESPP shall continue in effect under the 2009 ESPP, but in accordance with the terms of the 2001 ESPP. There will be 1.5 million shares of our common stock authorized for issuance under the 2009 ESPP if it is approved by stockholders. Upon the stockholders' approval of the 2009 ESPP, no further shares will be authorized for issuance under the 2001 ESPP.

In this Proposal 3, stockholders are requested to approve the adoption of the 2009 ESPP. The affirmative vote of the holders of a majority of the shares of common stock present in person or represented by proxy and entitled to vote at the 2009 Annual Meeting will be required to approve the adoption of the 2009 ESPP. Abstentions will be counted toward the tabulation of votes cast on proposals presented to the stockholders and will have the same effect as negative votes. Broker non-votes are counted towards a quorum, but are not counted for any purpose in determining whether this matter has been approved.

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The following summary describes the principal features of the 2009 ESPP, and is qualified in its entirety by reference to the full text of the 2009 ESPP. A copy of the 2009 ESPP is filed as Appendix B to the proxy statement for the 2009 Annual Meeting filed with the SEC.

### **Participation in the 2009 ESPP**

Participation in the 2009 ESPP is voluntary and is dependent on each eligible employee's election to participate and his or her determination as to the level of payroll deductions. Accordingly, future purchases under the 2009 ESPP are not determinable. Non-employee directors are not eligible to participate in the 2009 ESPP.

### **Description of the 2009 ESPP**

The essential terms of the 2009 ESPP are summarized as follows:

*General.* The purpose of the 2009 ESPP is to provide employees with an opportunity to purchase our common stock through accumulated payroll deductions.

*Administration.* The 2009 ESPP may be administered by the Board of Directors, the Compensation Committee or another committee appointed by the Board. All questions of interpretation or application of the 2009 ESPP are determined by the Board of Directors or its appointed committee, and its decisions are final, conclusive and binding upon all participants. The Board of Directors or its appointed committee may, without regard to whether participant rights may be considered to have been adversely effected, change the duration of the Purchase Periods (as defined below) or the length or date of commencement of an Offering Period, limit the frequency and/or number of changes in the amount withheld during an Offering Period (as defined below), establish the exchange ratio applicable to amounts withheld in a currency other than US dollars, permit payroll withholding in excess of the amount designated by a participant in order to adjust for delays or mistakes in our processing of properly completed withholding elections, establish reasonable waiting and adjustment periods and/or accounting and crediting procedures to ensure that amounts applied toward the purchase of our common stock for each participant properly correspond with amounts withheld from the participant's compensation, and establish such other limitations or procedures as the Board of Directors or its appointed committee determines in its sole discretion advisable which are consistent with the 2009 ESPP.

*Eligibility.* Each of our employees (including officers) whose customary employment with us is at least 20 hours per week is eligible to participate in an Offering Period; provided, however, that no employee shall be granted an option under the 2009 ESPP (i) to the extent that, immediately after the grant, such employee would own capital stock and/or hold outstanding options to purchase such stock representing five percent or more of the voting power or value of our stock, or (ii) to the extent that his or her rights to purchase stock under all of our employee stock purchase plans accrue at an amount which exceeds \$25,000 worth of common stock (determined at the fair market value of the shares at the time such option is granted) for each calendar year in which such option is outstanding at any time. Eligible employees become participants in the 2009 ESPP by filing with us an authorization form authorizing payroll deductions prior to the beginning of each Offering Period unless a later time for filing the authorization form has been set by the Board of Directors. As of April 24, 2009, approximately 425 employees were eligible to participate in the 2009 ESPP. These employees include (i) our six executive officers and (ii) approximately 130 employees selected for a reduction in force that is expected to be substantially completed by June 22, 2009.

*Participation in an Offering.* The 2009 ESPP is implemented by consecutive, overlapping offering periods lasting for 24 months (an Offering Period), with a new Offering Period commencing on the first trading day on or after January 1, April 1, July 1 and October 1 of each year. Common stock may be purchased under the 2009 ESPP every three months (a Purchase Period), unless the participant withdraws or terminates employment earlier. To the extent the fair market value of our common stock on any exercise date in an Offering Period is lower than the fair market value of our common stock on the first trading day of the Offering Period, then all participants in such Offering Period will be automatically withdrawn from such Offering Period immediately.

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after the exercise of their options on such exercise date and automatically re-enrolled in the immediately following Offering Period as of the first day thereof. To participate in the 2009 ESPP, each eligible employee must authorize payroll deductions pursuant to the 2009 ESPP. Such payroll deductions may not exceed 15% of a participant's compensation.

Once an employee becomes a participant in the 2009 ESPP, the employee will automatically participate in each successive Offering Period until such time as the employee withdraws from the 2009 ESPP or the employee's employment with us terminates. At the beginning of each Offering Period, each participant is automatically granted an option to purchase shares of our common stock. The option expires at the end of the Offering Period or upon termination of employment, whichever is earlier, but is exercised at the end of each Purchase Period to the extent of the payroll deductions accumulated during such Purchase Period. The number of shares subject to the option may not exceed 625 shares of our common stock in each Purchase Period.

All Offering Periods existing under the 2001 ESPP on the effective date of the 2009 ESPP will continue under the 2009 ESPP, but in accordance with the terms of the 2001 ESPP, including with respect to their Purchase Price and duration. The shares reserved for issuance under the 2009 ESPP will be available for purchase with respect to Offering Periods existing under the 2001 ESPP on the effective date of the 2009 ESPP and those commencing at any time under the 2009 ESPP.

*Purchase Price; Shares Purchased.* Shares of our common stock may be purchased under the 2009 ESPP at a price not less than 85% of the lesser of the fair market value of our common stock on the (i) the first trading day of each Offering Period or (ii) the last trading day of each Purchase Period (the Purchase Price). The fair market value of our common stock on any relevant date will generally be the closing price per share as quoted on the NASDAQ Stock Market (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported). The number of shares of our common stock a participant purchases in each Purchase Period is determined by dividing the total amount of payroll deductions withheld from the participant's compensation during that Purchase Period by the Purchase Price. On April 24, 2009, the closing price as reported on the NASDAQ Global Market was \$2.46 per share.

*Restrictions on Transfer.* Rights granted under the 2009 ESPP are not transferable and may be exercised only by the person to whom such rights are granted.

*Termination of Employment.* Termination of a participant's employment for any reason, including disability or death, or the failure of the participant to remain in our continuous scheduled employ for at least 20 hours per week, cancels his or her option and participation in the 2009 ESPP immediately. In such event, the payroll deductions credited to the participant's account will be returned to him or her or, in the case of death, to the person or persons entitled thereto as provided in the 2009 ESPP.

*Adjustment upon Change in Capitalization.* In the event of any stock split, reverse stock split, stock dividend, extraordinary cash dividend, combination, reclassification or other change in our capital structure affected without the receipt of consideration, appropriate proportional adjustments shall be made in the number and class of shares of stock subject to the 2009 ESPP, the number of shares of stock subject to options outstanding under the 2009 ESPP and the exercise price of any such outstanding options, and the maximum number of shares that each participant may purchase during each Purchase Period. Any such adjustment shall be made by the Board of Directors or its appointed committee, whose determination shall be final, binding and conclusive.

*Dissolution or Liquidation.* In the event of a proposed dissolution or liquidation, the Offering Period then in progress will be shortened and a new exercise date will be set.

*Merger or Asset Sale.* In the event we merge with or into another corporation or a sale of all or substantially all of our assets, each outstanding option may be assumed or substituted by the successor

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corporation. If the successor corporation refuses to assume or substitute the outstanding options, any Offering Periods then in progress will be shortened and a new exercise date will be set.

*Amendment and Termination of the Plan.* The Board of Directors may at any time terminate or amend the 2009 ESPP. An Offering Period may be terminated by the Board of Directors at the end of any Purchase Period if the Board determines that termination of the Offering Period or the 2009 ESPP is in the best interests of the company and our stockholders. No amendment shall be effective unless it is approved by the holders of a majority of the votes cast at a duly held stockholders' meeting, if such amendment would require stockholder approval to comply with Section 423 of the Code, stock exchange rules or other applicable law. Unless terminated earlier, the 2009 ESPP will terminate on June 25, 2019.

*Withdrawal.* Generally, a participant may withdraw from an Offering Period at any time without affecting his or her eligibility to participate in future Offering Periods. However, once a participant withdraws from a particular offering, that participant may not participate again in the same offering.

*Federal Tax Information for the 2009 ESPP.* The 2009 ESPP, and the right of participants to make purchases thereunder, is intended to qualify under the provisions of Sections 421 and 423 of the Code. A participant is taxed on amounts withheld for the purchase of shares as if such amounts were actually received. Other than this, no income will be taxable to a participant until the shares purchased under the 2009 ESPP are sold or otherwise disposed of. Upon sale or other disposition of the shares, the participant will generally be subject to tax and the amount of the tax will depend upon the holding period.

If the shares sold or disposed of have been held more than one year from the date of transfer of the stock to the participant and more than two years from the first day of the Offering Period, or in the event of a participant's death (whenever occurring), then the participant (or, if applicable, the participant's beneficiary) will recognize ordinary income equal to the lesser of (i) 15% of the value of the shares as of the first day of the Offering Period, or (ii) the excess of the value of the shares at the time of such sale or disposition over the price to the participant. Any additional gain or loss will be treated as long-term capital gain or loss.

If the shares sold or disposed of have not been held for the respective one or two year required holding periods, then the participant will recognize ordinary income generally measured as the excess of the value of the shares on the date the shares are purchased over the price to the participant. Any additional gain or loss on such sale or disposition will be long- or short-term capital gain or loss, depending on the holding period. We are not entitled to a deduction for amounts taxed to a participant except to the extent ordinary income is recognized by participants upon a sale or disposition of shares prior to the expiration of the holding periods described above.

The foregoing is only a summary of the effect of federal income taxation upon the participant and us with respect to the shares purchased under the 2009 ESPP. In addition, this summary does not discuss the tax consequences of a participant's death or the income tax laws of any state or foreign country in which the participant may reside. Reference should be made to the applicable provisions of the Code for more complete details.

***THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE APPROVAL OF THE 2009 EMPLOYEE STOCK PURCHASE PLAN.***



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**Approval of an Amendment to Our Fifth Amended and Restated Certificate of Incorporation to Increase Authorized Shares of Stock  
(Proposal 4)**

On April 17, 2009 our Board of Directors adopted, subject to stockholder approval, an amendment to our Fifth Amended and Restated Certificate of Incorporation, as amended, to increase the total number of our authorized shares from 150.0 million to 250.0 million, and to increase the number of authorized shares of our common stock from 142.5 million to 242.5 million (the Certificate Amendment ).

Stockholders are requested in this Proposal 4 to approve the Certificate Amendment. The affirmative vote of the holders of a majority of the shares of common stock outstanding will be required to approve the Certificate Amendment. Abstentions and broker non-votes will have the same effect as a vote against the Certificate Amendment.

The additional common stock to be authorized by adoption of the Certificate Amendment would have rights identical to our currently outstanding common stock. Adoption of the Certificate Amendment and issuance of our common stock would not affect the rights of the holders of our currently outstanding common stock. However, there may be ancillary effects incidental to increasing the number of shares of our common stock outstanding, such as dilution of earnings per share and voting rights of current holders of common stock. If the Certificate Amendment is adopted, it will become effective upon filing of a Certificate of Amendment to our Fifth Amended and Restated Certificate of Incorporation, as amended, with the Secretary of State of the State of Delaware.

In addition to the 80,029,891 shares of common stock outstanding on April 17, 2009, the following shares were reserved as of such date: (i) an aggregate of 9,671,835 shares of our common stock for issuance under our equity compensation plans; (ii) 107,919 shares for issuance under our deferred compensation plan; (iii) 2,655 shares for issuance under the 2001 ESPP; and (iv) 2,030,253 shares for issuance upon the exercise of outstanding warrants. Additional shares of common stock would be reserved for issuance under the 2009 LTIP and 2009 ESPP, as more fully described under Proposals 2 and 3, if such plans are approved by stockholders.

Although our Board of Directors has no other plans to issue the additional shares of common stock, it desires to have the shares available to provide additional flexibility to use capital stock for business and financial purposes in the future. The additional shares may be used for various purposes without further stockholder approval. These purposes may include: raising capital; providing equity incentives to employees, directors, consultants and/or advisors; establishing strategic relationships with other companies; expanding our business through the acquisition of other businesses or products; and other purposes. The additional shares of common stock that would become available for issuance if this proposal is adopted could also be used by us to oppose a hostile takeover attempt or to delay or prevent changes in our control or management. For example, without further stockholder approval, our Board of Directors could strategically sell shares of common stock in a private transaction to purchasers who would oppose a takeover or favor our then current Board. This proposal to increase the authorized common stock has been prompted by business and financial considerations and not by the threat of any hostile takeover attempt or any effort of which we are aware to accumulate our stock or to obtain control of Arena (nor is our Board of Directors currently aware of any such attempts directed at us). Nevertheless, stockholders should be aware that approval of this proposal could facilitate future efforts by us to deter or prevent changes in our control, including transactions in which the stockholders might otherwise receive a premium for their shares over then current market prices. We do not currently intend to use the additional shares of common stock to oppose a hostile takeover attempt or to delay or prevent changes in control of management.

***THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE AMENDMENT TO OUR FIFTH AMENDED AND RESTATED CERTIFICATE OF INCORPORATION.***

**Table of Contents****Securities authorized for issuance under equity compensation plans**

The following table summarizes our compensation plans under which our equity securities are authorized for issuance as of December 31, 2008.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders*	8,506,730	\$ 7.51	1,317,598**
Equity compensation plans not approved by security holders			
<b>Total*</b>	<b>8,506,730</b>	<b>\$ 7.51</b>	<b>1,317,598**</b>

\* Includes 6,556,630 stock options with a per share weighted-average exercise price of \$9.74 and 1,950,100 performance-based restricted stock unit awards which have no per share weighted-average exercise price. Excludes 29,000 shares of unvested restricted stock and 107,919 shares of restricted stock contributed to a deferred compensation plan by certain of our executive officers that were previously granted under an equity compensation plan approved by our stockholders.

\*\* Includes 92,493 shares of common stock available for future issuance under our 2001 ESPP.

**Compensation and Other Information****Concerning Executive Officers, Directors and Certain Stockholders****Security Ownership of Certain Beneficial Owners and Management**

The following table sets forth certain information known to us with respect to the beneficial ownership of our common stock as of April 24, 2009 by:

Each person, group or entity who is the beneficial owner of 5% or more of our common stock;

Each director and nominee for director;

Our Named Executive Officers; and

All current directors and executive officers as a group.

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Unless otherwise indicated in the footnotes below, the address for the beneficial owners listed in this table is in care of Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121. This table is based on information supplied by executive officers, directors and principal stockholders and Schedules 13D, 13G and other filings made with the SEC. Unless otherwise indicated in the footnotes to this table and subject to community property laws where applicable, we believe that the stockholders named in this table have sole voting and investment power with respect to the shares indicated as beneficially owned. Applicable percentages are based on 80,030,641 shares of common stock outstanding on April 24, 2009, including 2,000 restricted shares of common stock, and as adjusted as required by the rules promulgated by the SEC. This table includes shares issuable pursuant to stock options and other rights to purchase shares of our common stock exercisable within 60 days of April 24, 2009.

Name and Address of Beneficial Owner	Shares Beneficially Owned	Percentage of Total
Federated Investors, Inc. (1)	8,861,935	11.1%
Wellington Management Company, LLP (2)	8,124,217	10.2%
OppenheimerFunds, Inc. (3)	6,155,057	7.7%
Entities affiliated with Deerfield Capital, L.P. (4)	5,288,505	6.6%
Entities affiliated with Barclays Global Investors, NA (5)	4,416,033	5.5%
Jack Lief (6)	1,227,232	1.5%
Dominic P. Behan, Ph.D. (7)	714,448	*
Steven W. Spector, J.D. (8)	275,563	*
Robert E. Hoffman, C.P.A. (9)	199,349	*
J. Clayburn La Force, Jr., Ph.D. (10)	186,396	*
William R. Shanahan, Jr., M.D., J.D. (11)	163,750	*
Harry F. Hixson, Jr., Ph.D. (12)	148,810	*
Donald D. Belcher (13)	133,800	*
Scott H. Bice (14)	77,292	*
Tina S. Nova, Ph.D. (15)	72,000	*
Christine A. White, M.D. (16)	68,768	*
Phillip M. Schneider (17)	35,324	*
Randall E. Woods (18)	25,324	*
All directors and executive officers as a group (14 persons) (19)	3,409,682	4.1%

\* Less than one percent

- (1) The principal business office of Federated Investors, Inc. is Federated Investors Tower, 1001 Liberty Avenue, Pittsburgh, Pennsylvania 15222.
- (2) The principal business office of Wellington Management Company, LLP is 75 State Street, Boston, Massachusetts 02109.
- (3) OppenheimerFunds, Inc., a registered investment adviser, had shared voting and dispositive power with respect to all 6,155,057 shares, including the 6,000,000 shares owned by the Oppenheimer Global Opportunities Fund. Oppenheimer Global Opportunities Fund, an investment company registered under Section 8 of the Investment Company Act of 1940, had shared voting and dispositive power with respect to 6,000,000 shares. OppenheimerFunds, Inc. disclaims beneficial ownership as an investment adviser. The principal business office of OppenheimerFunds, Inc. is Two World Financial Center, 225 Liberty Street, New York, NY 10281.
- (4) Represents shares held by Deerfield Capital, L.P., Deerfield Partners, L.P., Deerfield International Limited, Deerfield Management Company, L.P., and James E. Flynn. The principal business office of Deerfield Capital, L.P., Deerfield Partners, L.P., Deerfield Management Company, L.P., and James E. Flynn is 780 Third Avenue, 37<sup>th</sup> Floor, New York, New York 10017. The principal business office of Deerfield International Limited is c/o Bisy Management, Bison Court, Columbus Centre, P.O. Box 3460, Road Town, Tortola,

British Virgin Islands.

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- (5) Represents shares held by Barclays Global Investors, NA and Barclays Global Fund Advisors. The principal business office of Barclays Global Investors, NA and Barclays Global Fund Advisors is 400 Howard Street, San Francisco, California 94105.
- (6) Includes 698,850 shares issuable to Mr. Lief upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (7) Includes 318,948 shares issuable to Dr. Behan upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (8) Includes 220,000 shares issuable to Mr. Spector upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (9) Includes 141,250 shares issuable to Mr. Hoffman upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (10) Includes 176,396 shares issuable to Dr. La Force upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (11) Includes 163,750 shares issuable to Dr. Shanahan upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (12) Includes 118,810 shares issuable to Dr. Hixson upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (13) Includes 118,800 shares issuable to Mr. Belcher upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (14) Includes 76,192 shares issuable to Mr. Bice upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (15) Includes 72,000 shares issuable to Dr. Nova upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (16) Includes 68,768 shares issuable to Dr. White upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (17) Includes 25,324 shares issuable to Mr. Schneider upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (18) Includes 25,324 shares issuable to Mr. Woods upon the exercise of stock options that are exercisable within 60 days of April 24, 2009.
- (19) Includes 2,301,912 shares issuable upon the exercise of stock options held by our directors and executive officers that are exercisable within 60 days of April 24, 2009.

**Table of Contents****Executive Officers**

Our executive officers are appointed by our Board of Directors and serve at the discretion of our Board. The following table sets forth information as of April 24, 2009 regarding our executive officers.

Name	Age	Position
Jack Lief	63	Chairman, President and Chief Executive Officer
K.A. Ajit-Simh	56	Vice President, Quality Systems
Dominic P. Behan, Ph.D.	45	Senior Vice President and Chief Scientific Officer
Robert E. Hoffman, C.P.A.	43	Vice President, Finance and Chief Financial Officer
William R. Shanahan, Jr., M.D., J.D.	60	Vice President and Chief Medical Officer
Steven W. Spector, J.D.	44	Senior Vice President, General Counsel and Secretary

See Election of Directors (*Proposal 1*) for biographical information regarding Mr. Lief and Dr. Behan, who are also directors.

K.A. Ajit-Simh has served as our Vice President, Quality Systems since January 2004. Mr. Ajit-Simh provided regulatory compliance services to several companies in the United States and internationally from 1999 to the end of 2003. Mr. Ajit-Simh held various positions of increasing responsibility at Mallinckrodt Inc., a pharmaceutical/chemical company, from 1975 to 1985, Baxter Healthcare, a health products company, from 1986 to 1989, Abbott BioTech, a health products company, from 1989 to 1992, and Cytel Corporation, a biotechnology company, from 1992 to 1999. In addition, Mr. Ajit-Simh has been an instructor at the University of California, San Diego since 1994, teaching classes in regulatory compliance and quality control/assurance. Mr. Ajit-Simh also teaches courses in Good Manufacturing Practices and Advanced Quality Control and Assurance at San Diego State University as part of the graduate program in Regulatory Affairs. Mr. Ajit-Simh received a B.Sc. degree in Biology and Chemistry from Bangalore University and an M.S. in Cell Biology from St. Louis University.

Robert E. Hoffman, C.P.A., has served as our Vice President, Finance and Chief Financial Officer since December 2005. Mr. Hoffman served as our Vice President, Finance and Chief Accounting Officer from June 2004 to December 2005, as our Vice President, Finance from April 2000 to June 2004, and as our Controller from August 1997 to April 2000. From 1994 to 1997, Mr. Hoffman served as Assistant Controller for Document Sciences Corporation, a software company. Mr. Hoffman serves as a member of the steering committee of the Association of Bioscience Financial Officers and as a supervisory committee member of the San Diego County Credit Union. Mr. Hoffman is also a director and a former President of the San Diego chapter of Financial Executives International. Mr. Hoffman holds a B.B.A. from St. Bonaventure University and is licensed as a C.P.A. in the State of California.

William R. Shanahan, Jr., M.D., J.D., has served as our Vice President and Chief Medical Officer since March 2004. From August 2000 to March 2004, Dr. Shanahan served as Chief Medical Officer for Tanox, Inc., a biopharmaceutical company. From October 1994 to August 2000, Dr. Shanahan held various positions at Isis Pharmaceuticals, Inc., a biopharmaceutical company, most recently as Vice President, Drug Development. From 1989 to 1994, Dr. Shanahan served as Director, Clinical Research for Pfizer Central Research, a pharmaceutical company. From 1986 to 1989, Dr. Shanahan held various positions at Searle Research & Development, a pharmaceutical company subsequently acquired by Pfizer, most recently as Director, Clinical Research. Dr. Shanahan holds an A.B. from Dartmouth College, an M.D. from the University of California, San Francisco and a J.D. from Loyola University, Chicago.

Steven W. Spector, J.D., has served as our Senior Vice President and General Counsel since June 2004. Mr. Spector served as our Vice President and General Counsel from October 2001 to June 2004. Mr. Spector has also served as our Secretary since November 2001. Mr. Spector is a member of the board of directors and a former President of the Association of Corporate Counsel, San Diego. Prior to joining Arena, Mr. Spector was a partner with the law firm of Morgan, Lewis & Bockius LLP, where he worked from 1991 to October 2001.

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Mr. Spector was our outside corporate counsel from 1998 to October 2001. Mr. Spector holds a B.A. and a J.D. from the University of Pennsylvania.

### **Compensation Discussion and Analysis**

#### ***Introduction***

This section provides an overview and analysis of our executive officer compensation program and policies, material compensation decisions we have made under such program and policies, and material factors that we considered in making those decisions. Later in this proxy statement, you will find a series of tables containing specific information about the compensation earned or paid in 2008 to the following individuals, whom we refer to as our Named Executive Officers: Messrs. Lief, Hoffman and Spector and Drs. Behan and Shanahan. The below discussion is intended to help you understand the detailed information provided in those tables and to put that information into context with our overall executive officer compensation program.

#### ***Executive Officer Compensation Philosophy, Objectives and Development***

We believe that the performance of our executive officers has the potential to significantly impact our ability to achieve our corporate goals. We, therefore, place considerable importance on the design and administration of our executive officer compensation program. This program is intended to enhance stockholder value by attracting, motivating and retaining qualified individuals to perform at the highest of professional levels and to contribute to our growth and success. Accordingly, our executive officer compensation program is designed to provide executive officers with compensation opportunities that are tied to their individual performance, as well as our overall corporate performance. Each executive officer's compensation package is comprised of three key elements: (i) base salary, (ii) performance-based cash incentives and (iii) stock-based compensation. Our executive officers are also entitled to health and welfare benefits, and, as discussed below, certain of them may be entitled to receive additional benefits upon termination of their employment. These additional elements of executive compensation, together with the three key elements, are intended to align the interests of our executive officers with those of our stockholders.

Our compensation packages are also designed to be competitive in our industry. The Compensation Committee may consult with compensation consultants, legal counsel and other advisors in designing our compensation program, including in relation to our corporate goals and in evaluating the competitiveness of individual compensation packages. In such evaluation, the Compensation Committee periodically reviews and analyzes executive officer compensation provided by other companies in our industry.

Our overall compensation philosophy is to pay our executive officers base annual salary that is at approximately the median level relative to a selected peer group of companies and to provide opportunities, through cash and equity incentives, to attain above the median total compensation relative to our peer group if we satisfy certain key performance goals. The main principles of our compensation strategy include the following:

Compensation decisions are driven by a pay-for-performance philosophy;

Compensation should be tied to both corporate and individual performance; and

Higher than median compensation can be earned through an executive officer's and the company's extraordinary performance. As part of the process for setting executive compensation, our Chief Executive Officer provides the Compensation Committee with his performance assessments of the company and our executive officers. He also recommends to the Compensation Committee salaries, cash incentive opportunities, cash incentive awards and equity grants for executive officers other than himself. The Compensation Committee can accept, reject or modify such recommendations in its discretion. The Compensation Committee also considers the recommendations of its independent consultant, peer company data, Southern California and national industry



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compensation surveys, and factors such as the past, current and expected contributions of each executive officer, our corporate performance, global economic conditions, the mix of compensation that would be most appropriate for each executive officer and the executive officer's particular responsibilities, experience, level of accountability and decision authority.

While the Compensation Committee meets regularly in executive session, various members of management, including our Chief Executive Officer, Chief Financial Officer and General Counsel, and other employees as well as outside advisors or consultants may be invited by the Compensation Committee to make presentations, provide financial or other background information or advice or otherwise participate in Compensation Committee meetings. Our General Counsel attends meetings of the Compensation Committee as the Secretary. Our Chief Executive Officer is not present during any deliberations or determinations of the Compensation Committee regarding his compensation.

In determining our executive officers' cash incentive awards for 2008 and developing the 2009 executive compensation program, the Compensation Committee considered what it viewed, in light of the global economic challenges, as a difficult year for us in terms of our stock performance, but also our success in meeting key preset goals and the importance of keeping our executive officers focused on corporate and individual goals that the committee believes will increase stockholder value.

The Compensation Committee has retained Frederic W. Cook & Co., Inc., as its independent compensation consultant from time to time since 2003 to advise it regarding compensation matters, including our compensation programs for directors and executive officers. The Compensation Committee retained such consultant in the second half of 2008 to assist in (i) reviewing the competitiveness and structure of our compensation program for executive officers, (ii) reviewing our current equity incentive plans and (iii) developing the new long-term incentive plan and employee stock purchase plan that are being proposed in this proxy statement. Frederic W. Cook & Co., Inc., did not perform any other work for us during 2008.

The compensation consultant's findings and recommendations regarding compensation are based in part on market data from a peer group of biotechnology and biopharmaceutical companies, which changes from time to time based on corporate developments, including clinical and commercial progress, affecting us and other companies in our industry. The Compensation Committee selects the peer group in consultation with its compensation consultant and other members of the Board of Directors, including our Chief Executive Officer, and taking into account our and the selected companies' development stages, market capitalizations, revenues, employees and earnings.

*2007 Peer Group.* In determining the number and type of equity awards to grant to executive officers in 2007, around the end of 2006, the Compensation Committee updated our peer group. This 2007 peer group consisted of the following companies: Cell Genesys, Inc., Connetics Corporation, Dendreon Corporation, Enzo Biochem, Inc., Exelixis, Inc., Human Genome Sciences, Inc., InterMune, Inc., Isis Pharmaceuticals, Inc., Lexicon Pharmaceuticals, Inc., Medarex, Inc., The Medicines Company, Noven Pharmaceuticals, Inc., Nuvelo, Inc., Onyx Pharmaceuticals, Inc., Senomyx, Inc., Telik, Inc., and Trimeris, Inc. The Compensation Committee referred to the 2007 peer group in determining the 2008 option awards for our executive officers.

*2008 Peer Group.* Around the end of 2008, the Compensation Committee again updated our peer group. This 2008 peer group consisted of the following companies: Cell Genesys, Inc., Dendreon Corporation, Dyax Corp., Enzo Biochem, Inc., Enzon Pharmaceuticals, Inc., Exelixis, Inc., Geron Corporation, Human Genome Sciences, Inc., Infinity Pharmaceuticals, Inc., InterMune, Inc., Isis Pharmaceuticals, Inc., Lexicon Pharmaceuticals, Inc., Medarex, Inc., The Medicines Company, Noven Pharmaceuticals, Inc., Progenics Pharmaceuticals, Inc., Theravance, Inc., and XOMA Ltd. The Compensation Committee referred to the 2008 peer group in (i) determining the 2009 option awards and 2009 cash compensation for our executive officers and (ii) developing our 2009 Annual Incentive Plan for our executive officers.

**Table of Contents****Elements of Our Compensation Program****1. Base Salary**

We generally target base annual salaries to be at approximately the market median of our peer group for executive officers having similar responsibilities, but the salary for any particular executive officer may be higher or lower than the market median depending on such factors as the individual's overall mix of base salary, performance-based cash incentives and stock-based compensation, the individual's historical base salary, the individual's experience and background, the individual's past performance and expected future contribution, the movement of salaries in the marketplace, and our corporate performance during the prior year. The purpose of base salary is to provide fixed compensation to attract and retain an employee with the qualifications desired for the particular position. Our philosophy is to make what we view as modest increases in salary for executive officers, except where an individual's salary is found to be significantly below market when compared to the selected peer group, and to use equity and performance-based cash compensation to further motivate and retain our executive officers. The Compensation Committee did not engage its compensation consultant in determining the 2008 base salaries for executive officers, but rather relied on its consultant's 2005-2006 report, its consultant's view that the committee could continue to rely on such report, and more recent industry surveys. The consultant's 2005-2006 report was based on a peer group that consisted of the following companies: Antigenics Inc., Arqule, Inc., CancerVax Corporation, Cell Genesys, Inc., Cell Therapeutics, Inc., Connetics Corporation, Curagen Corporation, Dendreon Corporation, Enzo Biochem, Inc., Exelixis, Inc., Guilford Pharmaceuticals, Inc., InterMune, Inc., Isis Pharmaceuticals, Inc., Lexicon Pharmaceuticals, Inc., Maxim Pharmaceuticals, Inc., Medarex, Inc., Noven Pharmaceuticals, Inc., Trimeris, Inc., and XOMA, Ltd.

**2. Performance-based cash incentives**

In early 2008, the Compensation Committee approved the 2008 Annual Incentive Plan for our executive officers. Under this cash incentive plan, each participant was assigned an incentive target that was expressed as a percentage of annual base salary, and the participant's incentive award was based on the achievement of preestablished corporate and individual goals. All participants had the same corporate goals, which we believed would align the interests of our executive officers with one another and with our stockholders. The corporate and individual goals were approved by the Compensation Committee after taking into account the views and recommendations of other members of our Board of Directors (including our Chief Executive Officer), which also approved the corporate goals and the Chief Executive Officer's individual goals.

The corporate goals for 2008 related to the following categories: (i) development of internal clinical programs, (ii) progress of programs with partners, (iii) budget, finance and integration of new capabilities, and (iv) progress of research programs. Individual goals were tailored for each executive officer, and related to the following categories: (i) progress and milestones of programs, (ii) budget and finance, (iii) integration of new capabilities, (iv) compliance and risk mitigation, (v) corporate governance, (vi) corporate planning, (vii) strategic opportunities, (viii) intellectual property and (ix) investor and analyst relations. Corporate and individual goals were intended to reflect a mix of short- and long-term performance objectives.

All of our executive officers participated in the 2008 Annual Incentive Plan. The following table lists our Named Executive Officers, their incentive target under the plan expressed as a percentage of their annual base salary, and the relative weighting assigned to corporate and individual goals:

Named Executive Officer	Incentive Target	Relative Weighting	
		Corporate Goals	Individual Goals
Jack Lief	50%	75%	25%
Robert E. Hoffman, C.P.A.	35%	60%	40%
Dominic P. Behan, Ph.D.	35%	60%	40%
William R. Shanahan, Jr., M.D., J.D.	30%	50%	50%
Steven W. Spector, J.D.	35%	60%	40%

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The Compensation Committee took into account its compensation consultant's recommendations, market data and individual performance and contribution in determining the incentive targets and relative weightings. The weighting of corporate versus individual goals was intended to reflect the participants' responsibilities for their individual areas and the company-wide functions. Mr. Lief's goals were weighted more heavily to the corporate goals than any other of our Named Executive Officers due to his role in overseeing our company-wide functions as our Chairman, President and Chief Executive Officer, and Dr. Shanahan's goals were weighted more to his individual goals than the other Named Executive Officers due to his significant role in the development of our drug candidates as our Vice President and Chief Medical Officer. Our other Named Executive Officers' goals were weighted more heavily to the corporate goals as their responsibilities involved company-wide functions more than any individual area and to tie their compensation to corporate achievements.

The threshold level of aggregate goal achievement under the 2008 Annual Incentive Plan for each executive officer was 50%, below which no incentive award would be paid to the executive officer. This threshold was established to ensure that no awards would be paid if the results achieved were significantly below the target. The Compensation Committee sets goals that it believes will be difficult for our executive officers to fully achieve. Consequently, achieving the target was only expected to occur if both corporate and individual performances were high. For example, in determining incentive awards under the 2007 Annual Incentive Plan, the Compensation Committee determined that 80% of the weighted value of the 2007 corporate goals was achieved, and that, with regard to the 2007 individual goals, Messrs. Lief and Spector and Dr. Shanahan achieved 100% of the weighted value, Dr. Behan achieved 90% of the weighted value and Mr. Hoffman achieved 80% of the weighted value. Executive officers are eligible to receive incentive awards of up to 125% of the target amount, which allows the Compensation Committee discretion to award more than the target award for extraordinary performance.

The below "Grants of Plan-Based Awards" table shows the incentives that could have been earned under this incentive plan, and the awards earned are included in the below "Summary Compensation Table."

All executive officers achieved more than the threshold percentage of goals under the 2008 Annual Incentive Plan, but received less than the target incentive award. The Compensation Committee determined that 85% of the weighted value of the 2008 corporate goals was achieved, and that, with regard to the 2008 individual goals, Messrs. Lief and Spector and Dr. Behan achieved 100% of the weighted value, Mr. Hoffman achieved 83% of the weighted value and Dr. Shanahan achieved 94% of the weighted value. Based only on such percentages, the awards under the plan to our Named Executive Officers would have been as follows: Mr. Lief, \$297,313; Dr. Behan, \$123,897; Mr. Hoffman, \$88,550; Dr. Shanahan, \$92,901; and Mr. Spector, \$116,253. The Compensation Committee granted awards that were higher than such amounts after also considering the other components of the formula for incentive awards, which are the quality and level of the goal achievement. The Compensation Committee also took into account the additional difficulty in achieving the goals due to the global economic challenges that wasn't foreseen at the time the goals were established.

In early 2009, the Compensation Committee approved corporate and individual goals and a similar annual incentive plan, with the exception of increasing the incentive target percentages, for all of our executive officers for use in determining cash incentive awards for 2009. Based on recommendations of the Compensation Committee's compensation consultant and market data, the Compensation Committee increased the incentive target percentage for Mr. Lief to 55% and increased the incentive targets for our other Named Executive Officers to 40%.

**3. Stock-based compensation**

We believe that equity grants provide our executive officers with the opportunity to share in increases, if any, in the value of our common stock and encourage their ownership in our company. We believe that equity grants reinforce a long-term interest in our corporate performance and directly motivate our executive officers to maximize long-term stockholder value. The equity grants also utilize vesting and, in the case of stock options, exercisability periods that encourage executive officers to continue working for us.

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**Table of Contents***Stock Options*

For 2008, the Compensation Committee granted our executive officers stock options, which are intended to foster the long-term perspective we believe is necessary for continued success. In determining the size and types of equity grants to executive officers, the Compensation Committee considered the performance-based restricted stock units that it awarded executive officers in 2007, similar awards to individuals holding comparable jobs in our 2007 peer group, our corporate performance against our plan, the individual's performance against his goals, each executive officer's ownership in Arena, the overall share usage under our equity compensation plans for grants to our executive officers, the amount of equity that would be available for future issuance following the grants, the consequences of granting equity in light of the requirements to expense the value of equity grants and the tax efficiency of various award types. The Compensation Committee also considered the performance, role and responsibilities of each executive officer. Taking into account the 2007 performance-based restricted stock unit awards, the Compensation Committee's overall objective was to grant stock options that would place the executive officers' aggregate equity grants within the broad middle range of the long-term equity grants in our 2007 peer group.

Stock options provide for financial gain only if the price of our common stock increases above the exercise price, which is set at the closing price of our common stock on the date of grant as reported on the NASDAQ Global Market (or if there is no closing price on such date, on the last preceding date on which a closing price was reported). Stock options granted to employees vest 25% per year over four years after the date of grant and are exercisable for up to 10 years from the date of grant. We believe that the vesting restrictions help retain executive officers and that the 10-year exercise period provides incentive for our executive officers to execute on our long-term business plan. We generally make stock option grants to continuing employees, including executive officers, on an annual basis. Our policy is to make such grants three trading days after our announcement of financial results for the prior year. In addition, we generally make an initial stock option grant to new employees on a preset day in the month following the employee's date of hire.

All grants to executive officers require the approval of the Compensation Committee. The Compensation Committee may delegate to (i) a committee of one or more members of our Board of Directors the authority to take action on behalf of the Compensation Committee under the LTIP, including the right to grant, cancel, suspend or amend awards and (ii) one or more of our executive officers the right to grant awards to non-executive employees, advisors and consultants. The Compensation Committee has delegated to Mr. Lief the ability to grant up to an aggregate of 120,000 stock options to non-executive employees and consultants each quarter. It is the Compensation Committee's policy for Mr. Lief to report to it any such stock option grants at its next regularly scheduled committee meeting.

*2007 Performance-based Restricted Stock Unit Awards*

For 2007, in addition to stock options, the Compensation Committee granted performance-based restricted stock unit awards to executive officers and other employees. These awards were designed to encourage, and compensate our executive officers and other employees for achieving, extraordinary results and to ensure that our executive officers and other employees are properly focused on specific drug development and commercialization initiatives that we believe will enhance long-term stockholder value. These awards provide executive officers and other employees until February 26, 2012 to achieve four specific drug development and strategic performance goals. A fixed number of awards will be earned for each milestone that is successfully achieved. Once earned, the awards will remain unvested until the performance period is complete. The awards that have been earned at February 26, 2012 will vest and be settled in shares of our common stock, with the holder receiving one share of common stock for each award earned and vested. Termination of employment prior to vesting will result in the forfeiture of any earned (as well as unearned) awards, except for limited circumstances such as termination due to death, disability or a change in control. As of April 24, 2009, we had not achieved any of the four goals under the performance-based restricted stock unit awards.

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The performance goals were established to require significant efforts and results that are expected to drive significant stockholder value, if achieved, thereby further aligning employee and stockholder interests. Each of the performance goals is designed to be a significant milestone for us, the attainment of which is not assured.

Depending on whether we have achieved one, two, three or all four of the performance goals on or before February 26, 2012 and if the particular executive officer is still employed on such date, then these stock unit awards would vest as follows: 25% if one goal is achieved, 50% if two goals are achieved, 87.5% if three goals are achieved and 100% if all four goals are achieved.

Below are the number of performance-based restricted stock unit awards our Compensation Committee granted to our Named Executive Officers in February 2007. The Compensation Committee did not grant any performance-based restricted stock unit awards to our Named Executive Officers in 2008.

Named Executive Officer	Performance-based Restricted Stock Unit Awards (1)
Jack Lief	300,000
Robert E. Hoffman, C.P.A.	100,000
Dominic P. Behan, Ph.D.	100,000
William R. Shanahan, Jr., M.D., J.D.	80,000
Steven W. Spector, J.D.	100,000

(1) Maximum number that may be earned for achieving all four performance goals.  
*Employee Stock Purchase Plan*

We have adopted the 2001 ESPP as a further benefit to executive officers, as well as other employees, and to encourage employee ownership. Under the 2001 ESPP, participants may elect to have a portion of their cash compensation withheld for purchases of our common stock on certain dates set forth in the plan. The price of our common stock purchased under the 2001 ESPP is equal to 85% of the lower of the fair market value of our common stock on the date of enrollment or the exercise date of the purchase period.

**4. Other Benefits and Post-Termination Compensation**

All of our executive officers, as well as our other regular, full-time US employees, are eligible for a variety of health and welfare and paid time-off benefits. We believe that reliable and competitive health and welfare and paid time-off benefits help ensure that we have a productive and focused workforce.

*401(k) Plan and Company Match*

Our US employees are eligible to participate in our 401(k) plan beginning on their hire date. Employees may make pre-tax or after tax (Roth) contributions of up to 50% of gross cash compensation into the plan, up to the annual limit established by the IRS. Subject to limits established by the IRS, we match 100% of each of the employee's contributions, subject to a maximum match of 6% of the employee's gross cash compensation. This match vests over a five-year period from the individual's date of hire. Due to the current global economic environment and our financial condition, we intend to discontinue our match of 401(k) contributions, beginning on August 1, 2009.

*Life and Disability Coverage*

We provide all regular, full-time US employees with a life insurance policy equal to four times the employee's annual salary, up to a maximum coverage of \$500,000. Such employees are also covered by short- and long-term disability plans that coordinate with the California State Disability plan.

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### *Perquisites and Other Benefits*

We did not provide any of our Named Executive Officers or other senior members of management with perquisites in 2008 that exceeded \$10,000 in the aggregate for any person, and do not expect to do so in 2009.

### *Post-Termination Compensation*

We have entered into Termination Protection Agreements and have a Severance Benefit Plan that may require us to provide compensation and benefits to certain of our executive officers. The agreements and the plan are summarized below and more detail regarding potential payouts is provided below under Potential Post-Employment Payments Table.

*Termination Protection Agreements.* In 2002, we entered into Termination Protection Agreements because we determined that it was appropriate to provide certain of our executive officers severance compensation if there is a change in control and the executive officer's employment is terminated under certain circumstances. We did this to promote the ability of our executive officers to keep focused on corporate interests and to act in the best interests of our stockholders even though their employment could be terminated as a result of the change in control. These agreements were put into place after one of our stockholders acquired approximately 28% of our outstanding common stock. In addition, as part of our normal course of business, we engage in discussions with other companies about possible collaborations and other ways in which we may work together to further our respective long-term objectives and many larger, more established companies consider companies at similar stages of development to ours as potential acquisition targets.

*Severance Benefit Plan.* In 2006, the Compensation Committee approved the Severance Benefit Plan for certain executive officers. Separation benefits are payable if the executive officer's employment is terminated under certain circumstances and are intended to keep our executive officers focused on corporate interests while employed and to ease the consequences to an executive officer of a termination of employment. The advantage to us includes our receipt of a waiver and release of claims, which the separated executive officer must provide to us as a condition to receiving benefits. Any payments payable under the Severance Benefit Plan are reduced by severance benefits payable by us under the Termination Protection Agreements or any other agreement, policy, plan, program or arrangement.

On December 30, 2008, we amended and restated the Termination Protection Agreements and the Severance Benefit Plan, primarily to bring them into compliance with Section 409A of the Internal Revenue Code of 1986, as amended, and the regulations and other guidance promulgated thereunder, or Section 409A. The amendments to the Termination Protection Agreements, which require a change in control to trigger benefits, include (1) delaying cash payment until a date within five business days after the earlier of (i) the first business day that is six months following the employee's termination or (ii) following the employee's termination, the employee's death; (2) modifying the good reason definition relating to the relocation of the employee's principal office or place of business required to trigger the benefits; and (3) adding a waiver and release as a condition to receiving severance benefits. The amendments to the Severance Benefit Plan include (1) delaying cash payment until, within five business days after, the earlier of (i) the first business day that is six months following the employee's termination or (ii) following the employee's termination, the employee's death; (2) modifying the good reason definition relating to the relocation of the employee's principal office or place of business required to trigger the benefits; and (3) adding a deadline for turning in the waiver and release that is required as a condition to receiving severance benefits.

### *Tax Considerations*

We intend that all incentive payments be deductible for tax purposes unless it would undermine our ability to meet our primary compensation objectives. We also take into account the tax effects of various forms of compensation and the potential for excise taxes to be imposed on our executive officers. There are various

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provisions of the Internal Revenue Code of 1986, as amended, or the Code, which we consider in determining compensation, including the following:

*Section 162(m).* We consider the potential impact of Section 162(m) of the Code, which denies a Federal income tax deduction for any individual compensation exceeding \$1,000,000 in any taxable year for the chief executive officer and the three highest compensated executive officers other than the chief executive officer and chief financial officer. This limitation does not, however, apply to compensation that is performance-based under a plan that is approved by the stockholders and that meets other requirements. Based on these requirements, we attempt to limit the impact Section 162(m) will have on our ability to deduct compensation, but in appropriate circumstances we will pay compensation that is not deductible under Section 162(m) if necessary and in the best interests of our stockholders.

*Sections 280G and 4999.* Any payment or benefit provided under our Termination Protection Agreements or our Severance Benefit Plan in connection with a change-in-control transaction may be subject to an excise tax under Section 4999 of the Code. These payments also may not be eligible for a company tax deduction pursuant to Section 280G of the Code. If any of these payments or benefits are subject to the excise tax, they may be reduced to provide the individual with the best after-tax result. Specifically, the individual will receive either a reduced amount so that the excise tax is not triggered, or the individual will receive the full amount of the payments and benefits and then be liable for any excise tax.

## **Compensation Committee Report**

*This report of our Compensation Committee is not deemed to be soliciting material, or to be filed with the SEC or subject to the SEC's proxy rules (other than as provided in Item 407 of Regulation S-K) or to the liabilities of Section 18 of the Exchange Act, and, irrespective of any general incorporation language, this report shall not be deemed incorporated by reference into any prior or subsequent filing by us under the Securities Act of 1933 or the Exchange Act, except to the extent that we specifically incorporate it by reference into any such filing.*

The Compensation Committee, comprised of independent directors, reviewed and discussed the above Compensation Discussion and Analysis with our management. Based on such review and discussions, the Compensation Committee recommended to our Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement and included into our Annual Report on Form 10-K for the fiscal year ended December 31, 2008.

Donald D. Belcher

Scott H. Bice

Harry F. Hixson, Jr., Ph.D.

Christine A. White, M.D.

**Table of Contents****Summary Compensation Table for Fiscal Years Ended December 31, 2008, 2007 and 2006**

In January 2008, the Compensation Committee approved increases in annual base salary for each of our Named Executive Officers, such that Mr. Lief's annual base salary was increased from \$640,000 to \$670,000; Mr. Hoffman's annual base salary was increased from \$285,000 to \$300,000; Dr. Behan's annual base salary was increased from \$371,000 to \$389,000; Dr. Shanahan's annual base salary was increased from \$333,000 to \$346,000; and Mr. Spector's annual base salary was increased from \$340,000 to \$365,000. The following table summarizes the total compensation of our Named Executive Officers for the fiscal years ended December 31, 2008, 2007 and 2006.

Name and Principal Position	Year	Salary (\$)(1)	Stock Awards (\$)(2)	Option Awards (\$)(3)	Non-Equity Incentive Plan Compensation (\$)(4)	All Other Compensation (\$)(5)	Total (\$)
<b>Jack Lief</b>	2008	\$ 668,021	\$ 201,600	\$ 956,194	\$ 300,000	\$ 14,334	\$ 2,140,149
Chairman, President and Chief Executive Officer	2007	638,889	219,461	1,968,705(6)	325,000	14,034	3,166,089
	2006	619,431	399,133	404,907	260,000	13,734	1,697,205
<b>Robert E. Hoffman, C.P.A.</b>	2008	299,010	84,000	219,441	95,000	34,526(7)	731,977
Vice President, Finance and Chief Financial Officer	2007	284,444	84,000	218,461	90,000	30,476(7)	707,381
	2006	273,056	77,000	153,170	82,000	24,309(7)	609,535
<b>Dominic P. Behan, Ph.D.</b>	2008	387,813	84,000	319,585	125,000	14,334	930,732
Senior Vice President, Chief Scientific Officer and Director	2007	370,323	92,931	300,749	125,000	14,034	903,037
	2006	358,033	184,167	190,804	97,000	13,734	843,738
<b>William R. Shanahan, Jr., M.D., J.D.</b>	2008	345,142		232,290	95,000	14,334	686,766
Vice President and Chief Medical Officer	2007	332,356		229,571	90,000	14,034	665,961
	2006	320,878		149,386	75,000	13,734	558,998
<b>Steven W. Spector, J.D.</b>	2008	363,351	84,000	316,345	125,000	28,372(8)	917,068
Senior Vice President, General Counsel and Secretary	2007	339,312	84,000	297,509	125,000	33,649(8)	879,470
	2006	326,900	77,000	179,832	97,000	26,333(8)	707,065

- (1) In accordance with SEC rules, the compensation described in this table does not include medical or other benefits received by our Named Executive Officers that are available generally to all of our regular, full-time employees and certain perquisites and other personal benefits received by our Named Executive Officers which, in the aggregate, were less than \$10,000 for any officer. Amounts earned but deferred at the election of our Named Executive Officer pursuant to our 401(k) plan are included in the salary column.
- (2) Represents the dollar amount recognized for financial statement reporting purposes for the designated fiscal year in accordance with Statement of Financial Accounting Standards, or SFAS, No. 123R, Share-Based Payment, which includes amounts from stock awards granted prior to our adoption of SFAS No. 123R in 2006 as well as awards granted subsequent to such adoption.
- (3) Represents the dollar amount recognized for financial statement reporting purposes for the designated fiscal year in accordance with SFAS No. 123R, except that estimates of forfeitures related to vesting under SFAS No. 123R have been excluded. For the relevant assumptions used in determining these amounts, refer to Note 10 to our audited consolidated financial statements included in our annual report on Form 10-K as filed with the SEC on March 16, 2009, and Note 1 to our audited consolidated financial statements included in our annual report on Form 10-K as filed with the SEC on March 6, 2007.
- (4) Represents cash awards earned pursuant to our 2008, 2007 and 2006 Annual Incentive Plans, as further described below in the Grants of Plan-Based Awards table and the above Compensation Discussion and Analysis. For all years presented, cash awards earned were paid in the subsequent fiscal year.



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- (5) Represents matching contributions to our 401(k) plan made on behalf of our Named Executive Officers and life insurance premiums paid by us for our Named Executive Officers.

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(6) In June 2006, we began granting employee stock options that provide for continued vesting after an individual leaves the company if (i) the individual's employment is terminated other than for cause, (ii) such individual is at least 60 years old, and (iii) such individual has provided at least 10 years of service to the company. The stock options included in this table vest over a four-year period, but, as Mr. Lief is over 60 years old and has provided over 10 years of service to the company, in July 2007, we recorded the unrecognized compensation expense for all of the stock options granted to Mr. Lief between June 2006 and July 2007.

(7) Through the end of 2008, after their annual anniversary hire date, each of our employees could elect to be paid for unused vacation time in the form of additional salary, subject to certain limitations. In addition to items noted in footnote 5 above, these numbers reflect Mr. Hoffman's election to be paid \$20,192, \$16,442 and \$10,577 in the form of additional salary for unused vacation time in 2008, 2007 and 2006, respectively.

(8) In addition to items noted in footnote 5 above, these numbers reflect Mr. Spector's election to be paid \$14,038, \$19,615 and \$12,600 in the form of additional salary for unused vacation time in 2008, 2007 and 2006, respectively.

In January 2009, the Compensation Committee approved increases in annual base salaries for our Named Executive Officers, such that Mr. Lief's annual base salary was increased to \$690,000; Mr. Hoffman's annual base salary was increased to \$327,000; Dr. Behan's annual base salary was increased to \$400,000; Dr. Shanahan's annual base salary was increased to \$357,000; and Mr. Spector's annual base salary was increased to \$375,000.

**Table of Contents****Grants of Plan-Based Awards During Fiscal Year Ended December 31, 2008**

The following table provides information on estimated future payouts under non-equity incentive plans and stock options granted to our Named Executive Officers during the fiscal year ended December 31, 2008.

Name	Grant Date	Approval Date (2)	Estimated Future Payouts Under Non-Equity Incentive Plan Awards (1)			All Other Option Awards: Number of Securities Underlying Options (#) (3)	Exercise or Base Price of Option Awards (\$/sh) (4)	Grant Date Fair Value of Stock and Option Awards (\$) (5)
			Threshold (\$)	Target (\$)	Maximum (\$)			
<b>Jack Lief</b>	3/3/08	1/25/08	\$ 167,500	\$ 335,000	\$ 418,750	180,000	\$ 6.99	\$ 663,120
<b>Robert E. Hoffman, C. P. A.</b>	3/3/08	1/25/08	52,500	105,000	131,250	35,000	6.99	128,940
<b>Dominic P. Behan, Ph.D.</b>	3/3/08	1/25/08	68,075	136,150	170,188	60,000	6.99	221,040
<b>William R. Shanahan, Jr., M.D., J.D.</b>	3/3/08	1/25/08	51,900	103,800	129,750	45,000	6.99	165,780
<b>Steven W. Spector, J.D.</b>	3/3/08	1/25/08	63,875	127,750	159,688	60,000	6.99	221,040

- (1) Our 2008 Annual Incentive Plan was our only non-equity incentive plan in 2008. The amounts shown in the threshold column reflect the minimum payment level under our 2008 Annual Incentive Plan, which is 50% of the amount shown in the target column. The amounts shown in the maximum column are 125% of the respective target amounts. These amounts are based on each Named Executive Officer's 2008 annual salary.
- (2) We generally make stock option grants to continuing employees, including executive officers, on an annual basis. Our policy is to make such grants three trading days after our announcement of financial results for the prior year. Our Compensation Committee approves such grants in a meeting that precedes the grant date, and, in the case of these stock option grants, such meeting occurred on January 25, 2008.
- (3) All awards granted in 2008 were granted under our 2006 LTIP.
- (4) In all cases, the exercise price of such option awards was equal to the closing market price of our common stock on the grant date as reported on the NASDAQ Global Market.
- (5) Represents the full value of each award that would be recognized for financial statement reporting purposes over the applicable vesting period in accordance with SFAS No. 123R. For the relevant assumptions used in determining these amounts, refer to Note 10 to our audited consolidated financial statements included in our annual report on Form 10-K as filed with the SEC on March 16, 2009. The amount of these awards that was expensed in 2008 is included above under Summary Compensation Table.
- See Compensation Discussion and Analysis above for additional information regarding targets for payment of cash incentives, performance criteria on which cash incentives and the number of option awards were based and for additional information regarding our grant timing, dating and pricing policies.

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Individual cash incentive awards under our 2008 Annual Incentive Plan were determined in early 2009 based upon the extent to which goals were achieved, the quality of achievement and the weighting of each goal.

All stock options granted to our Named Executive Officers are incentive stock options to the extent permissible under the Code. All such stock options vest 25% per year over four years from the date of grant and are exercisable for up to 10 years from the date of grant.

**Table of Contents****Outstanding Equity Awards at Fiscal Year Ended December 31, 2008**

The following table provides information on all stock options and any unvested stock awards held by our Named Executive Officers on December 31, 2008.

Name	Option Awards				Stock Awards			Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$) (3)
	Number of Securities Underlying Unexercised Options (#) Exercisable (1)	Number of Securities Underlying Unexercised Options (#) Unexercisable (1)	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#) (2)	Market Value of Shares or Units of Stock That Have Not Vested (\$) (3)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#) (4)	
<b>Jack Lief</b>	70,000		\$ 16.00	1/16/11				\$
	170,000		12.25	1/15/12				
					12,000	50,040		
	100,000		6.00	1/18/14				
	124,350		6.16	1/17/15				
	89,000		16.80	1/20/16				
	10,500	10,500	10.52	7/28/16				
	45,000	135,000	13.50	2/26/17				
	180,000	6.99	3/3/18			75,000	312,750	
<b>Robert E. Hoffman, C.P.A.</b>	5,000		12.25	1/15/12				
	40,000		6.00	1/18/14				
	30,000		6.16	1/17/15				
	40,000		16.80	1/20/16				
	8,750	26,250	13.50	2/26/17	5,000	20,850		
	35,000	6.99	3/3/18			25,000	104,250	
<b>Dominic P. Behan, Ph.D.</b>	87,500		0.60	3/3/10				
	50,000		24.23	8/22/10				
	85,000		12.25	1/15/12				
	33,332		6.00	1/18/14				
	33,116		6.16	1/17/15				
	40,000		16.80	1/20/16				
	5,000	5,000	10.52	7/28/16	5,000	20,850		
15,000	45,000	13.50	2/26/17					
	60,000	6.99	3/3/18			25,000	104,250	
<b>William R. Shanahan, Jr., M.D., J.D.</b>	60,000		6.30	4/18/14				
	45,000		6.16	1/17/15				
	25,000		16.80	1/20/16				
	11,250	33,750	13.50	2/26/17				
		45,000	6.99	3/3/18			20,000	83,400
<b>Steven W. Spector, J.D.</b>	35,000		9.05	9/26/11				
	50,000		6.00	1/18/14				
	45,000		6.16	1/17/15				
	40,000		16.80	1/20/16				

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	5,000	5,000	10.52	7/28/16	5,000	20,850		
	15,000	45,000	13.50	2/26/17				
		60,000	6.99	3/3/18			25,000	104,250

- (1) Generally stock options vest 25% per year over four years from the date of grant and are exercisable for up to 10 years from the date of grant. All stock options granted prior to the approval of our 2006 LTIP on June 12, 2006 were granted

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pursuant to stock option plans that allowed them to be exercised prior to vesting, subject to repurchase at the original exercise price in the event of termination. Our 2006 LTIP does not allow stock options to be exercised prior to vesting.

- (2) These restricted shares vested on January 20, 2009. Subject to certain restrictions on transferability and a risk of forfeiture, the Named Executive Officer has all rights of a stockholder as of the date of grant. Unvested shares of restricted common stock are subject to forfeiture in the event of termination of service.
- (3) Computed by multiplying the closing market price of our common stock on December 31, 2008 of \$4.17 by the number of shares or stock unit awards, as appropriate, that have not vested.
- (4) The amounts included in this column represent the number of shares earned upon achievement of the threshold performance goals for the performance-based restricted stock unit awards granted in February 2007, which is the achievement of one of the four milestones, or 25% of the total grant. As of April 24, 2009, we have not achieved any of the four goals under the performance-based restricted stock unit awards. See 2007 Performance-based Restricted Stock Unit Awards in the above Compensation Discussion and Analysis for additional information.

**Option Exercises and Stock Vested During Fiscal Year Ended December 31, 2008**

The following table provides information on stock awards vested during the fiscal year ended December 31, 2008.

Name	Stock Awards	
	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$ (1))
<b>Jack Lief</b>	12,000	\$ 94,560
<b>Robert E. Hoffman, C.P.A.</b>	5,000	39,400
<b>Dominic P. Behan, Ph.D.</b>	5,000	39,400
<b>William R. Shanahan, Jr., M.D., J.D.</b>		
<b>Steven W. Spector, J.D.</b>	5,000	39,400
-		

- (1) Computed by multiplying the number of shares vested by the closing market price of our common stock on the vesting date.

**Table of Contents****Nonqualified Deferred Compensation Table for Fiscal Year Ended December 31, 2008**

In 2003, we established a deferred compensation plan for our executive officers, whereby they may elect to defer the shares of restricted stock we have awarded them. Shares deferred in the plan become restricted stock units. This deferral opportunity was established in part to encourage the participants to continue to hold rights to own common stock in the future that may otherwise be sold to satisfy the participant's tax withholding or other financial obligations upon vesting, and for the purpose of rewarding and incentivizing the participants. Participants can choose to receive distributions under the plan as a lump sum distribution or in installments. A participant's election to defer restricted stock under the plan is irrevocable, but the participant may modify their election to provide for a later distribution date, add additional shares under the plan or to provide for a different form of distribution. In addition, the plan allows for hardship withdrawals, early withdrawals with a penalty, and withdrawals by beneficiaries following the death of a participant. Also, unless in connection with a change in control, no distributions are permitted under the plan to a participant in any taxable year to the extent such distribution would result in the participant receiving an amount of compensation that cannot be deducted by us pursuant to the limitations imposed on the deduction of certain compensation payments under Section 162(m) of the Code. At December 31, 2008, 107,919 shares of restricted stock were held in the deferred compensation plan, and the following table provides information about the activity in the deferred compensation plan as of December 31, 2008.

Name	Aggregate Earnings in Last FY (\$ (1))	Aggregate Balance at Last FYE (\$ (2))
<b>Jack Lief</b>		
<b>Robert E. Hoffman, C.P.A.</b>	\$ (68,625)	\$ 78,188
<b>Dominic P. Behan, Ph.D.</b>	(289,759)	330,135
<b>William R. Shanahan, Jr., M.D., J.D.</b>		
<b>Steven W. Spector, J.D.</b>		

-

- (1) Any earnings in the last fiscal year represent a change in the closing market price of our common stock. Neither the company nor any of the Named Executive Officers made withdrawals from or additional contributions to the deferred compensation plan in 2008. Accordingly, the amounts included in this column are not included in 2008 compensation in the above Summary Compensation Table.
- (2) Aggregate balance at last fiscal year-end was computed by multiplying the closing market price of our common stock on December 31, 2008 of \$4.17 by the number of shares issuable under the deferred compensation plan. An aggregate of \$120,563 and \$509,057 was previously reported as compensation in previous years' summary compensation tables for Mr. Hoffman and Dr. Behan, respectively.

**Potential Post-Employment Payments Table as of Fiscal Year Ended December 31, 2008**

Messrs. Lief, Hoffman and Spector and Dr. Behan, who are all of our Named Executive Officers that were employed by us in 2002, are each a party to a Termination Protection Agreement, dated December 20, 2002, as amended. Under the Termination Protection Agreements, if the participating executive officer is terminated without cause or resigns for good reason (as defined in the agreement) within two years following a change of control or if the executive officer is terminated within one year prior to a change in control in anticipation of the change in control, we are required to provide such executive officer (i) a payment equal to the executive officer's annual compensation, (ii) continuation of health insurance coverage until the second anniversary of the executive officer's termination, (iii) accelerated vesting of all outstanding unvested stock options and restricted shares, with any stock options remaining exercisable until as late as the first anniversary of the executive officer's termination, and (iv) continuation of our indemnification obligations until at least the sixth anniversary of the executive officer's termination. The cash severance benefits are equal to (i) the executive officer's annual rate of base salary in effect on the date of the change in control or the termination date, whichever is higher, and (ii) any



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bonus paid or payable to the executive officer for the year preceding the change in control or the termination date, whichever is higher. Following our receipt of an effective waiver and release of claims, we are required to pay the cash benefits in a lump sum within five business days after the earlier of (i) the first business day that is six months following the executive officer's termination or (ii) following the executive officer's termination, the executive officer's death.

We maintain a Severance Benefit Plan that provides Messrs. Lief, Hoffman and Spector and Drs. Behan and Shanahan severance benefits upon involuntary termination without cause or voluntary termination with good reason (as defined in the plan). The benefits include cash severance benefits, continuation of health insurance coverage for the severance period, acceleration of stock options and awards that would otherwise have vested through the end of the severance period, and continued stock option exercisability until the later of (i) the original post-termination exercise period provided in the applicable stock option agreement or (ii) the number of months equal to the severance period (but not beyond the original contractual life of the option). The cash severance benefits are equal to the number of months in the executive officer's severance period multiplied by the executive officer's monthly base salary in effect immediately prior to the termination plus one-twelfth of the greater of (i) the average of the three annual bonuses we paid to the executive officer prior to his termination and (ii) the last annual bonus paid to the executive officer prior to termination. Following our receipt of an effective waiver and release of claims and return of company property, we are required to pay the cash benefits in a lump sum within five business days after the earlier of (i) the first business day that is six months following the executive officer's termination or (ii) following the executive officer's termination, the executive officer's death. The severance period is 18 months for Mr. Lief and 12 months for the other included executive officers. Any payments payable under the Severance Benefit Plan are reduced by severance benefits payable by us under the Termination Protection Agreements or any other agreement, policy, plan, program or arrangement.

As described in the above Compensation Discussion and Analysis, on December 30, 2008, we amended and restated the Termination Protection Agreements and the Severance Benefit Plan, primarily to bring them into compliance with Section 409A.

In accordance with SEC rules, the below table provides information on the amounts payable upon termination of our Named Executive Officers assuming the triggering event (which would be their separation) took place on December 31, 2008. Information on certain tax implications of post-termination payments is included above under Tax Considerations.

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Name and Benefit	Termination Protection Agreement (Change in Control Required)	Severance Benefit Plan (No Change in Control Required)	Total Potential Payable Upon Termination(1)
<b>Jack Lief</b>			
Salary	\$ 670,000	\$ 1,005,000	\$ 1,005,000
Bonus	325,000	487,500	487,500
Benefit continuation	24,963	18,722	24,963
Accelerated vesting of restricted stock (2)	50,040	50,040	50,040
Accelerated vesting of stock options (3)			
Total	1,070,003	1,561,262	1,567,503
<b>Robert E. Hoffman, C.P.A.</b>			
Salary	300,000	300,000	300,000
Bonus	95,000	90,667	95,000
Benefit continuation	34,444	17,222	34,444
Accelerated vesting of restricted stock (2)	20,850	20,850	20,850
Accelerated vesting of stock options (3)			
Total	450,294	428,739	450,294
<b>Dominic P. Behan, Ph.D.</b>			
Salary	389,000	389,000	389,000
Bonus	125,000	125,000	125,000
Benefit continuation	34,444	17,222	34,444
Accelerated vesting of restricted stock (2)	20,850	20,850	20,850
Accelerated vesting of stock options (3)			
Total	569,294	552,072	569,294
<b>William R. Shanahan, Jr., M.D., J.D.</b>			
Salary		346,000	346,000
Bonus		90,000	90,000
Benefit continuation		17,222	17,222
Accelerated vesting of restricted stock (2)			
Accelerated vesting of stock options (3)			
Total		453,222	453,222
<b>Steven W. Spector, J.D.</b>			
Salary	365,000	365,000	365,000
Bonus	125,000	125,000	125,000
Benefit continuation	34,444	17,222	34,444
Accelerated vesting of restricted stock (2)	20,850	20,850	20,850
Accelerated vesting of stock options (3)			
Total	545,294	528,072	545,294

(1) Any payments payable under the Severance Benefit Plan are reduced by severance benefits payable by us under the Termination Protection Agreements or any other agreement, policy, plan, program or arrangement.

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- (2) No accelerated vesting of performance-based restricted stock unit awards is included since none of the performance goals were achieved on December 31, 2008 when the triggering event was assumed to take place.
  
- (3) Computed by multiplying the difference between the closing market price of our common stock on December 31, 2008 of \$4.17 and the exercise price of each stock option vested as a result of the termination by the number of accelerated stock options.

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### **Director Compensation**

The compensation for our non-employee directors is set forth below. Directors who are also employees do not receive additional compensation for serving as a director.

#### ***2008 Fiscal Year***

For fiscal year 2008, each of our non-employee directors was eligible to earn the following compensation for their participation on our Board of Directors and its committees:

#### ***Equity:***

*New Directors:* 18,000 options to purchase shares of our common stock. The options are 10-year options with an exercise price equal to the closing price of our common stock on the grant date as reported by the NASDAQ Global Market, vesting in equal annual installments over two years.

*Ongoing Directors:* 12,000 options to purchase shares of our common stock. The options are 10-year options with an exercise price equal to the closing price of our common stock on the grant date as reported by the NASDAQ Global Market, vesting in equal monthly installments over one year.

New director grants are made in connection with the new director's appointment to the Board of Directors and the annual grants are made to ongoing directors three trading days after our announcement of our prior year's financial results. For directors that did not serve for the full fiscal year preceding an annual grant, the grant is pro-rated based on the number of months such director served as a director in the prior year, if any.

Except in the case of a director's death or disability, unvested stock options under the 2006 LTIP terminate when the director ceases to be a director. Unless earlier terminated, vested stock options terminate three years after the director ceases to be a director (or, if applicable, an employee) for any reason other than the director's death or disability. In the event of a director's death or disability, the director's stock options become fully vested and exercisable and may be exercised within the earlier of three years after the date of the director's death or disability, as applicable, or the end of the 10-year term of the stock options.

#### ***Cash:***

*Retainer:* \$20,000 annually, paid quarterly, subject to continuing service as a director. Prior to the beginning of any calendar year or, in the case of a new director, to the extent permitted, upon joining our Board of Directors, each director can irrevocably elect to take 25%, 50%, 75% or 100% of his or her annual retainer, or, in the case of a new director, his or her pro rata retainer in (i) deferred stock units, or DSUs, on a \$1-for-\$1 basis, (ii) stock options to purchase a number of shares of stock determined by dividing three times the retainer amount elected by the fair market value of our common stock, computed at the time the stock options are granted, or (iii) a combination of cash, DSUs and options. The options are 10-year options with an exercise price equal to the closing price of our common stock on the grant date as reported by the NASDAQ Global Market, vesting in approximately equal monthly installments over one year.

If a director joins the Board of Directors after the first quarter of a calendar year, such director's retainer for that calendar year is reduced pro rata on a quarterly basis.

#### ***Meeting Attendance Fees:***

General:

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In-Person: \$1,000

Telephonic: \$500

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Exceptions:

Audit Chair Meeting Attendance Fee:

In-Person: \$3,000

Telephonic: \$1,500

Other Chair Meeting Attendance Fee:

In-Person: \$2,000

Telephonic: \$1,000

In addition, our Board of Directors and the Compensation Committee may authorize additional fees for significant work in informal meetings or for other service to us in the recipient's capacity as a director or committee member. Each non-employee director is also entitled to reimbursement for all of such director's reasonable out-of-pocket expenses incurred in connection with performing Board business.

**Director Compensation Table for Fiscal Year Ended December 31, 2008**

As described more fully above, the following table summarizes the compensation for our non-employee directors during the fiscal year ended December 31, 2008.

<b>Name</b>	<b>Fees Earned or Paid in Cash \$(1)</b>	<b>Option Awards \$(2)</b>	<b>Total (\$)</b>
Donald D. Belcher (3)	\$ 52,500	\$ 66,482	\$ 118,982
Scott H. Bice (4)	46,500	55,155	101,655
Harry F. Hixson, Jr., Ph.D. (5)	42,000	66,482	108,482
J. Clayburn La Force, Jr., Ph.D. (6)	41,000	66,482	107,482
Tina S. Nova, Ph.D. (7)	37,500	51,373	88,873
Phillip M. Schneider (8)	51,500	50,342	101,842
Christine A. White, M.D. (9)	45,500	117,626	163,126
Randall E. Woods (10)	40,000	50,342	90,342

- (1) For each director, includes all meeting attendance fees and the cash retainer earned or paid for the fiscal year ended December 31, 2008, whether or not the director elected to receive his or her cash retainer in cash, stock options or a combination of both.
- (2) Represents the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2008 in accordance with SFAS No. 123R, Share-Based Payment, which includes amounts from options granted in and prior to 2008, except that estimates of forfeitures related to vesting under SFAS No. 123R have been excluded. For the relevant assumptions used in determining these amounts, refer to Note 10 to our audited consolidated financial statements included in our annual report on Form 10-K as filed with the SEC on March 16, 2009.

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- (3) Mr. Belcher elected to receive 100% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Mr. Belcher in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 12,000 options granted to Mr. Belcher in 2008 was \$44,208. Mr. Belcher had a total of 112,060 options outstanding at December 31, 2008. \$12,000 of the meeting fees earned in 2007 and included above were paid to Mr. Belcher in 2008, and \$5,000 of the meeting fees earned in 2008 and included above were paid to Mr. Belcher in 2009.

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- (4) Mr. Bice elected to receive 25% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the \$5,000 portion of his annual retainer amount by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 2,146 options granted to Mr. Bice in 2008 in lieu of cash was \$7,906, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 12,000 options granted to Mr. Bice in 2008 was \$44,208. Mr. Bice had a total of 72,257 options outstanding at December 31, 2008. \$11,000 of the meeting fees earned in 2007 and included above were paid to Mr. Bice in 2008, and \$3,000 of the meeting fees earned in 2008 and included above were paid to Mr. Bice in 2009.
- (5) Dr. Hixson elected to receive 100% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Dr. Hixson in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 12,000 options granted to Dr. Hixson in 2008 was \$44,208. Dr. Hixson had a total of 112,070 options outstanding at December 31, 2008. \$10,000 of the meeting fees earned in 2007 and included above were paid to Dr. Hixson in 2008, and \$2,000 of the meeting fees earned in 2008 and included above were paid to Dr. Hixson in 2009.
- (6) Dr. La Force elected to receive 100% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Dr. La Force in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 12,000 options granted to Dr. La Force in 2008 was \$44,208. Dr. La Force had a total of 169,656 options outstanding at December 31, 2008. \$12,500 of the meeting fees earned in 2007 and included above were paid to Dr. La Force in 2008, and \$1,000 of the meeting fees earned in 2008 and included above were paid to Dr. La Force in 2009.
- (7) The grant-date fair value of the 12,000 options granted to Dr. Nova in 2008 was \$44,208. Dr. Nova had a total of 69,000 options outstanding at December 31, 2008. \$7,000 of the meeting fees earned in 2007 and included above were paid to Dr. Nova in 2008, and \$3,000 of the meeting fees earned in 2008 and included above were paid to Dr. Nova in 2009.
- (8) Mr. Schneider elected to receive 100% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Mr. Schneider in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 18,000 and 1,000 options granted to Mr. Schneider in 2008 was \$78,646 and \$3,684, respectively. Mr. Schneider had a total of 27,584 options outstanding at December 31, 2008. \$1,000 of the meeting fees and \$5,000 of the cash retainer earned in 2007 and included above were paid to Mr. Schneider in 2008, and \$7,000 of the meeting fees earned in 2008 and included above were paid to Mr. Schneider in 2009.
- (9) Dr. White elected to receive 100% of her annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Dr. White in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 12,000 options granted to Dr. White in 2008 was \$44,208. Dr. White had a total of 62,028 options outstanding at December 31, 2008. \$9,500 of the meeting fees earned in 2007 and included above were paid to Dr. White in 2008, and \$4,000 of the meeting fees earned in 2008 and included above were paid to Dr. White in 2009.



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(10) Mr. Woods elected to receive 100% of his annual cash retainer for the fiscal year ended December 31, 2008 in stock options determined by dividing three times the annual retainer amount of \$20,000 by the fair market value of our common stock, computed at the time the stock options were granted. The grant-date fair value of the 8,584 options granted to Mr. Woods in 2008 in lieu of cash was \$31,623, computed in accordance with SFAS No. 123R. Only the vested portion of the incremental value of these stock options is included in the option awards column. The grant-date fair value of the additional 18,000 and 1,000 options granted to Mr. Woods in 2008 was \$78,646 and \$3,684, respectively. Mr. Woods had a total of 27,584 options outstanding at December 31, 2008. \$1,000 of the meeting fees and \$5,000 of the cash retainer earned in 2007 and included above were paid to Mr. Woods in 2008, and \$4,000 of the meeting fees earned in 2008 and included above were paid to Mr. Woods in 2009.

All stock options granted to non-employee directors in the fiscal year ended December 31, 2008 were 10-year options with an exercise price equal to the closing market price of our common stock on the date of grant, vesting in approximately equal monthly installments over one year.

See Compensation Discussion and Analysis above for additional information regarding our grant timing, dating and pricing policies and the discussion above under 2008 Fiscal Year regarding the 2008 compensation for our non-employee directors.

***2009 Fiscal Year***

Beginning in fiscal year 2009, the Compensation Committee (i) eliminated the non-employee directors' ability to receive DSUs in lieu of their annual cash retainers, and, for 2009 only, (ii) limited to 20,000 the maximum number of options that may be issued to any director in lieu of their cash retainers. If the number of options resulting from a director's election would be limited by such maximum, then any portion of the retainer not converted into options because of such maximum will be paid in cash on the applicable quarterly retainer payment dates. We otherwise expect that our 2009 compensation for non-employee directors will be substantially similar to the compensation for 2008.

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**Audit Committee**

**Audit Committee Report**

*This report of our Audit Committee is not deemed to be soliciting material, or to be filed with the SEC or subject to the SEC's proxy rules (other than as provided in Item 407 of Regulation S-K) or to the liabilities of Section 18 of the Exchange Act, and, irrespective of any general incorporation language, this report shall not be deemed incorporated by reference into any prior or subsequent filing by us under the Securities Act of 1933 or the Exchange Act, except to the extent that we specifically incorporate it by reference into any such filing.*

Our management has the primary responsibility for our financial reporting process, accounting principles and internal controls as well as the preparation of our financial statements. The Audit Committee oversees our financial reporting process on behalf of our Board of Directors.

In fulfilling its responsibilities, the Audit Committee appointed Ernst & Young LLP, an independent registered public accounting firm, as our independent auditors for the 2008 fiscal year. The Audit Committee reviewed and discussed with the independent auditors the overall scope and specific plans for their audit. The Audit Committee also reviewed and discussed with the independent auditors and with management our audited consolidated financial statements and the adequacy of our internal control over financial reporting. The Audit Committee met with the independent auditors, without management present, to discuss the results of the independent auditors' audit, the independent auditors' evaluations of our internal control over financial reporting, and the overall quality of our financial reporting. The meetings were also designed to facilitate any desired private communication between the Audit Committee and the independent auditors.

The Audit Committee monitored the independence and performance of the independent auditors. The Audit Committee discussed with the independent auditors the matters required to be discussed by the Statement on Auditing Standards No. 114 (The Auditor's Communications with Those Charged with Governance), as adopted by the Public Company Accounting Oversight Board, or PCAOB, in Rule 3200T. The Audit Committee received the written disclosures and the letter from the independent auditors required by applicable requirements of the PCAOB regarding the independent accountants' communications with the Audit Committee concerning independence, and discussed with the independent auditors the independent auditors' independence.

Based on the review and discussions referred to above, the Audit Committee recommended to our Board of Directors that the audited consolidated financial statements be included in our annual report on Form 10-K for the fiscal year ended December 31, 2008, as filed with the SEC. The Audit Committee has also appointed Ernst & Young LLP as our independent auditors for the fiscal year ending December 31, 2009.

The foregoing report is provided by the following directors, who constitute the Audit Committee:

Donald D. Belcher

Phillip M. Schneider

Randall E. Woods

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### **Independent Auditors Fees**

The following presents aggregate fees billed to us for the fiscal years ended December 31, 2008 and 2007 by Ernst & Young LLP, our independent auditors and principal outside accountants.

**Audit Fees.** Audit fees were \$557,400 and \$524,000 for the years ended December 31, 2008 and 2007, respectively.

**Audit-Related Fees.** Audit-related fees were \$77,388 and \$25,758 for the years ended December 31, 2008 and 2007, respectively. The fees in 2008 were primarily related to consultations regarding the accounting treatment and valuation for our Swiss subsidiary, Arena Pharmaceuticals GmbH's acquisition of certain drug product facility assets, Statement of Financial Accounting Standards No. 157 implementation, the warrant settlement with one of our warrant holders, and the accounting treatment for our Series B Convertible Preferred Stock. The fees in 2007 were primarily related to consultations regarding performance-based restricted stock unit awards, Financial Accounting Standards Board Interpretation No. 48, or FIN 48, and the sale and leaseback of certain of our real property.

**Tax Fees.** Tax fees were \$25,000 and \$58,727 for the years ended December 31, 2008 and 2007, respectively. The fees in 2008 were related to an Internal Revenue Code Section 382 study. The fees in 2007 were related to consultations relating to Internal Revenue Code Section 382, FIN 48 and international tax matters, including Arena Pharmaceuticals GmbH's acquisition of certain drug product facility assets.

**All Other Fees.** There were no fees billed in either of the years ended December 31, 2008 or 2007 for products or services provided by our independent auditors other than those disclosed above in this section.

### **Pre-approval Policies and Procedures**

The Audit Committee has adopted a policy and procedures for pre-approving all audit and non-audit services to be performed by our independent auditors. The policy requires pre-approval of all services rendered by our independent auditors either as part of the Audit Committee's approval of the scope of the engagement of the independent auditors or on a case-by-case basis. The Audit Committee has authorized its Chair to pre-approve individual expenditures of audit and non-audit services. Any pre-approval decision must be reported to the Audit Committee at the next regularly scheduled Audit Committee meeting. The Audit Committee approved all audit, audit-related and tax fees for 2008 and 2007.

### **Ratification of Independent Auditors (Proposal 5)**

The Audit Committee has appointed Ernst & Young LLP, an independent registered public accounting firm, as our independent auditors for the fiscal year ending December 31, 2009. Ernst & Young LLP has audited our financial statements since our inception in 1997. Our Board of Directors is submitting the appointment of Ernst & Young LLP to the stockholders for ratification as a matter of good corporate practice.

In connection with the audit of the 2008 financial statements, we entered into an engagement letter with Ernst & Young LLP that sets forth the terms by which Ernst & Young LLP will perform audit services for us. The agreement is subject to alternative dispute resolution procedures and an exclusion of punitive damages.

Stockholders are requested in this Proposal 5 to ratify the appointment of Ernst & Young LLP. The affirmative vote of the holders of a majority of the shares of common stock present at the meeting in person or by proxy and entitled to vote will be required to ratify the appointment of Ernst & Young LLP. Abstentions will be counted toward the tabulation of votes cast on proposals presented to the stockholders and will have the same effect as negative votes. Broker non-votes are counted towards a quorum, but are not counted for any purpose in determining whether this matter has been approved.

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In the event that the stockholders fail to ratify the appointment, the Audit Committee will reconsider its selection of our independent auditors, but may decide not to change its selection. Even if the appointment is ratified, the Audit Committee may appoint different independent auditors at any time if it determines that such a change would be in the stockholders' best interest.

Representatives of Ernst & Young LLP are expected to be present at our 2009 Annual Meeting. They will have the opportunity to make a statement if they desire to do so, and will be available to respond to appropriate questions.

***THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE RATIFICATION OF THE APPOINTMENT OF ERNST & YOUNG LLP TO SERVE AS OUR INDEPENDENT AUDITORS FOR THE FISCAL YEAR ENDING DECEMBER 31, 2009.***

### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Exchange Act requires our directors, executive officers and our 10% or greater stockholders to file reports of ownership of our equity securities and changes in such ownership with the SEC and NASDAQ and to furnish us with copies of such reports.

To our knowledge, based on a review of the copies of such reports furnished to us and written representations that no other reports were required, all Section 16(a) filing requirements applicable to our directors, executive officers and our 10% or greater stockholders were complied with during the fiscal year ended December 31, 2008.

### **Stockholder Proposals for the 2009 Annual Meeting**

To be considered for inclusion in our proxy statement for next year's annual meeting, stockholder proposals must be in writing, addressed to our Corporate Secretary, and be received at our executive offices at 6166 Nancy Ridge Drive, San Diego, California 92121, no later than the close of business on January 15, 2010. In addition, notice of any stockholder proposal to be presented at next year's annual meeting of stockholders must be received at our executive offices no later than March 6, 2010, and no earlier than February 14, 2010. The above dates in this section may change under circumstances set forth in our Bylaws or if we amend the relevant provisions in our Bylaws. If we amend our Bylaws, we will file the amended Bylaws with the SEC. Stockholders may request a copy of the bylaw provisions relating to stockholder proposals from our Corporate Secretary at the same address.

Notices of intention to present proposals at the 2009 annual meeting of stockholders should be addressed to our Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121. We reserve the right to reject, rule out of order, or take appropriate action with respect to any proposal that does not comply with these and any other applicable requirements.

### **Annual Report**

A copy of our Annual Report for the 2008 fiscal year has been mailed concurrently with this proxy statement to all stockholders entitled to notice of and vote at our 2009 Annual Meeting. The Annual Report is not incorporated into this proxy statement and is not considered proxy solicitation material.

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**Annual Report on Form 10-K**

WE WILL MAIL WITHOUT CHARGE, UPON WRITTEN REQUEST, A COPY OF OUR ANNUAL REPORT ON FORM 10-K, INCLUDING THE FINANCIAL STATEMENTS, SCHEDULES AND LIST OF EXHIBITS. WE WILL FURNISH A COPY OF ANY EXHIBIT TO SUCH REPORT UPON WRITTEN REQUEST AND PAYMENT OF OUR REASONABLE EXPENSES IN FURNISHING SUCH EXHIBIT. REQUESTS SHOULD BE SENT TO INVESTOR RELATIONS, ARENA PHARMACEUTICALS, INC., 6166 NANCY RIDGE DRIVE, SAN DIEGO, CALIFORNIA 92121. OUR SEC FILINGS ARE ALSO AVAILABLE ON OUR WEBSITE AT [WWW.ARENAPHARM.COM](http://WWW.ARENAPHARM.COM).

**Householding of Proxy Materials**

The SEC has adopted rules that permit companies and intermediaries (such as brokers) to satisfy the delivery requirements for proxy statements and annual reports with respect to two or more stockholders sharing the same address by delivering a single proxy statement addressed to those stockholders. This process, which is commonly referred to as householding, potentially results in a reduced usage of natural resources and cost savings for companies.

A number of brokers with account holders who are our stockholders will be householding our proxy materials. A single proxy statement and one annual report will be delivered to multiple stockholders sharing an address unless contrary instructions have been received from the affected stockholders. Once you have received notice from your broker that they will be householding communications to your address, householding will continue until you are notified otherwise or until you revoke your consent. Any stockholder at a shared address to which a single copy of the documents was delivered and who wishes to receive a separate copy of the documents can request a copy of the documents by sending a written request to Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121, or contact our Corporate Secretary at 858.453.7200. Also, if, at any time, you no longer wish to participate in householding and would prefer to receive a separate proxy statement and annual report in the future, please notify your broker or direct your written request to Corporate Secretary, Arena Pharmaceuticals, Inc., 6166 Nancy Ridge Drive, San Diego, California 92121, or contact our Corporate Secretary at 858.453.7200. Stockholders who currently receive multiple copies of the proxy statement at their address and would like to request householding of their communications should contact their broker.

**Other Matters**

Our Board of Directors knows of no other business that will be presented for consideration at our 2009 Annual Meeting. If other matters are properly brought before our 2009 Annual Meeting, however, it is the intention of the persons named in the accompanying proxy to vote the shares represented thereby on such matters in accordance with their best judgment.

Dated: May 15, 2009

By Order of our Board of Directors

Steven W. Spector

*Senior Vice President, General Counsel and Secretary*

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**APPENDIX A**

**ARENA PHARMACEUTICALS, INC.**

**2009 LONG-TERM INCENTIVE PLAN**

Arena Pharmaceuticals, Inc. (the *Company*), a Delaware corporation, hereby establishes and adopts the following 2009 Long-Term Incentive Plan (the *Plan*).

**1. PURPOSE OF THE PLAN**

The purpose of the Plan is to assist the Company and its Affiliates in attracting and retaining selected individuals to serve as directors, employees, consultants and/or advisors of the Company and its Affiliates who are expected to contribute to the Company's success and achieve long-term objectives that will inure to the benefit of all stockholders of the Company through the additional incentives inherent in the Awards hereunder.

**2. DEFINITIONS**

**2.1.** *Affiliate* shall mean, at the time of determination, any parent or subsidiary of the Company as such terms are defined in Rule 405 of the Securities Act. The Board or the Committee shall have the authority to determine the time or times at which parent or subsidiary status is determined within the foregoing definition.

**2.2.** *Award* shall mean any Option, Stock Appreciation Right, Restricted Stock Award, Restricted Stock Unit Award, Performance Award or any other right, interest or option relating to Shares or other property (including cash) granted pursuant to the provisions of the Plan.

**2.3.** *Award Agreement* shall mean any written agreement, contract or other instrument or document evidencing any Award granted hereunder, including through an electronic medium.

**2.4.** *Board* shall mean the board of directors of the Company.

**2.5.** *Code* shall mean the Internal Revenue Code of 1986, as amended from time to time.

**2.6.** *Committee* shall mean the Compensation Committee of the Board or a subcommittee thereof formed by the Compensation Committee to act as the Committee hereunder. The Committee shall consist of no fewer than two Directors, each of whom is (i) a *Non-Employee Director* within the meaning of Rule 16b-3 of the Exchange Act, (ii) an *outside director* within the meaning of Section 162(m) of the Code, and (iii) an *independent director* for purpose of the rules of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded) to the extent required by such rules.

**2.7.** *Consultant* shall mean any consultant or advisor who is a natural person and who provides services to the Company or any Affiliate, so long as such person (i) renders bona fide services that are not in connection with the offer and sale of the Company's securities in a capital-raising transaction and (ii) does not directly or indirectly promote or maintain a market for the Company's securities.

**2.8.** *Covered Employee* shall mean an employee of the Company or its Affiliates who is a *covered employee* within the meaning of Section 162(m) of the Code.

**2.9.** *Director* shall mean a non-employee member of the Board.

**2.10.** *Dividend Equivalents* shall have the meaning set forth in Section 12.5.

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**2.11.** *Employee* shall mean any employee of the Company or any Affiliate and any prospective employee conditioned upon, and effective not earlier than, such person becoming an employee of the Company or any Affiliate.

**2.12.** *Exchange Act* shall mean the Securities Exchange Act of 1934, as amended.

**2.13.** *Fair Market Value* shall mean, with respect to Shares as of any date, (i) the per Share closing price of the Shares as reported on the NASDAQ Stock Market on that date (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported), (ii) if the Shares are not then listed on the NASDAQ Stock Market, the closing price on such other principal U.S. national securities exchange on which the Shares are listed (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported); or (iii) if the Shares are not listed on a U.S. national securities exchange, the Fair Market Value of Shares shall be determined by the Committee in its sole discretion using appropriate criteria. The Fair Market Value of any property other than Shares shall mean the market value of such property determined by such methods or procedures as shall be established from time to time by the Committee.

**2.14.** *Incentive Stock Option* shall mean an Option which when granted is intended to qualify as an incentive stock option for purposes of Section 422 of the Code.

**2.15.** *Limitations* shall have the meaning set forth in Section 10.5.

**2.16.** *Option* shall mean any right granted to a Participant under the Plan allowing such Participant to purchase Shares at such price or prices and during such period or periods as the Committee shall determine.

**2.17.** *Participant* shall mean an Employee, Director or Consultant who is selected by the Committee to receive an Award under the Plan.

**2.18.** *Payee* shall have the meaning set forth in Section 13.1.

**2.19.** *Performance Award* shall mean any Award of Performance Cash, Performance Shares or Performance Units granted pursuant to Article 9.

**2.20.** *Performance Cash* shall mean any cash incentives granted pursuant to Article 9 payable to the Participant upon the achievement of such performance goals as the Committee shall establish.

**2.21.** *Performance Period* shall mean that period established by the Committee at the time any Performance Award is granted or at any time thereafter during which any performance goals specified by the Committee with respect to such Award are to be measured.

**2.22.** *Performance Share* shall mean any grant pursuant to Article 9 of a unit valued by reference to a designated number of Shares, which value may be paid to the Participant by delivery of such property as the Committee shall determine, including cash, Shares, other property, or any combination thereof, upon achievement of such performance goals during the Performance Period as the Committee shall establish.

**2.23.** *Performance Unit* shall mean any grant pursuant to Section 9 of a unit valued by reference to a designated amount of property other than Shares (or cash), which value may be paid to the Participant by delivery of such property as the Committee shall determine, including cash, Shares, other property, or any combination thereof, upon achievement of such performance goals during the Performance Period as the Committee shall establish.

**2.24.** *Permitted Assignee* shall have the meaning set forth in Section 12.3.

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**2.25.** *Prior Plans* shall mean, collectively, the Company's Amended and Restated 1998 Equity Compensation Plan, Amended and Restated 2000 Equity Compensation Plan, 2002 Equity Compensation Plan and the 2006 Long-Term Incentive Plan, as amended. Awards granted under the Prior Plans continue to be governed under the terms of those Prior Plans.

**2.26.** *Restricted Stock* shall mean any Share issued with the restriction that the holder may not sell, transfer, pledge or assign such Share and with such other restrictions as the Committee, in its sole discretion, may impose (including any restriction on the right to vote such Share and the right to receive any dividends), which restrictions may lapse separately or in combination at such time or times, in installments or otherwise, as the Committee may deem appropriate.

**2.27.** *Restricted Stock Award* shall have the meaning set forth in Section 7.1.

**2.28.** *Restricted Stock Unit Award* shall have the meaning set forth in Section 8.1.

**2.29** *Restricted Stock Unit* means an Award that is valued by reference to a Share, which value may be paid to the Participant by delivery of cash, Shares or such other property as the Committee shall determine, which restrictions may lapse separately or in combination at such time or times, in installments or otherwise, as the Committee may deem appropriate.

**2.30.** *Shares* shall mean the shares of common stock, \$0.0001 par value, of the Company.

**2.31.** *Stock Appreciation Right* shall mean the right granted to a Participant pursuant to Section 6.

**2.32.** *Substitute Awards* shall mean Awards granted or Shares issued by the Company in assumption of, or in substitution or exchange for, awards previously granted, or the right or obligation to make future awards, in each case by a company acquired by the Company or any Affiliate or with which the Company or any Affiliate combines.

**2.33.** *Vesting Period* shall mean the period of time specified by the Committee during which vesting restrictions for an Award are applicable.

## **3. SHARES SUBJECT TO THE PLAN**

### **3.1 Number of Shares.**

(a) Subject to adjustment as provided in Section 12.2, a total of 7.0 million Shares shall be authorized for issuance under the Plan, as increased if applicable under this Section, less one (1) share of Stock for every one (1) share of Stock that was subject to an option or stock appreciation right granted after December 31, 2008 under the Prior Plans and 1.3 Shares for every one (1) Share that was subject to an award other than an option or stock appreciation right granted after December 31, 2008 under the Prior Plans. Any Shares that are subject to Awards other than Options or Stock Appreciation Rights shall be counted against this limit as 1.3 Shares for every one (1) Share granted. After the effective date of the Plan (as provided in Section 13.13), no awards may be granted under any Prior Plan.

(b) If (i) any Shares subject to an Award are forfeited, an Award expires or an Award is settled for cash (in whole or in part), or (ii) after December 31, 2008 any Shares subject to an award under the Prior Plans are forfeited, or an award under the Prior Plans expires or is settled for cash (in whole or in part), the Shares subject to such Award or award under the Prior Plans shall, to the extent of such forfeiture, expiration or cash settlement, again be available for Awards under the Plan, in accordance with Section 3.1(d) below. Notwithstanding anything to the contrary contained herein, the following Shares shall not be added to the Shares authorized for grant under paragraph (a) of this Section: (i) Shares tendered by the Participant or withheld by the Company in payment of the purchase price of an Option, or to satisfy any tax withholding



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obligation with respect to an Option or Stock Appreciation Right, (ii) Shares subject to a Stock Appreciation Right that are not issued in connection with the stock settlement of the Stock Appreciation Right on exercise thereof, and (iii) Shares reacquired by the Company on the open market or otherwise using cash proceeds from the exercise of Options or options granted under the Prior Plans.

(c) Shares issued under Substitute Awards shall not reduce the Shares authorized for grant under the Plan or the applicable Limitations authorized for grant to a Participant under Section 10.5, nor shall Shares subject to a Substitute Award again be available for Awards under the Plan to the extent of any forfeiture, expiration or cash settlement as provided in paragraph (b) above.

(d) Any Shares that again become available for grant pursuant to this Section shall be added back as (i) one (1) Share if such Shares were subject to Options or Stock Appreciation Rights granted under the Plan or options or stock appreciation rights granted under the Prior Plans, and (ii) as 1.3 Shares if such Shares were subject to Awards other than Options or Stock Appreciation Rights granted under the Plan or awards other than options or stock appreciation rights granted under the Prior Plans.

**3.2. *Character of Shares.*** Any Shares issued hereunder may consist, in whole or in part, of authorized and unissued shares, treasury shares or shares purchased in the open market or otherwise.

## **4. ELIGIBILITY AND ADMINISTRATION**

**4.1. *Eligibility.*** Any Employee, Director or Consultant shall be eligible to be selected as a Participant.

**4.2. *Administration.***

(a) The Plan shall be administered by the Committee. The Committee shall have full power and authority, subject to the provisions of the Plan and subject to such orders or resolutions not inconsistent with the provisions of the Plan as may from time to time be adopted by the Board, to: (i) select the Employees, Directors and Consultants to whom Awards may from time to time be granted hereunder; (ii) determine the type or types of Awards, not inconsistent with the provisions of the Plan, to be granted to each Participant hereunder; (iii) determine the number of Shares (or dollar value) to be covered by each Award granted hereunder; (iv) determine the terms and conditions, not inconsistent with the provisions of the Plan, of any Award granted hereunder (including the power to amend outstanding Awards); (v) determine whether, to what extent and under what circumstances Awards may be settled in cash, Shares or other property; (vi) determine whether, to what extent, and under what circumstances cash, Shares, other property and other amounts payable with respect to an Award made under the Plan shall be deferred either automatically or at the election of the Participant; (vii) determine whether, to what extent and under what circumstances any Award shall be canceled or suspended; (viii) interpret and administer the Plan and any instrument or agreement entered into under or in connection with the Plan, including any Award Agreement; (ix) correct any defect, supply any omission or reconcile any inconsistency in the Plan or any Award in the manner and to the extent that the Committee shall deem desirable to carry it into effect; (x) establish such rules and regulations and appoint such agents as it shall deem appropriate for the proper administration of the Plan; (xi) determine whether any Award, other than an Option or Stock Appreciation Right, will have Dividend Equivalents; and (xii) make any other determination and take any other action that the Committee deems necessary or desirable for administration of the Plan.

(b) Decisions of the Committee shall be final, conclusive and binding on all persons or entities, including the Company, any Participant, and any Affiliate. A majority of the members of the Committee may determine its actions, including fixing the time and place of its meetings.

(c) To the extent not inconsistent with applicable law, including Section 162(m) of the Code, or the rules and regulations of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded), the Committee may delegate to: (i) a committee of one or more members of the Board the authority to take action on behalf of the Committee under the Plan including the right to grant, cancel, suspend or amend Awards and (ii) one or more executive officers within the

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meaning of Rule 16a-1(f) of the Exchange Act or a committee of executive officers the right to grant Awards to Employees who are not executive officers of the Company and the authority to take action on behalf of the Committee pursuant to the Plan to cancel or suspend Awards to Employees who are not directors or executive officers of the Company.

(d) The Board in its discretion may ratify and approve actions taken by the Committee. In addition, to the extent not inconsistent with applicable law or the rules and regulations of the NASDAQ Stock Market or such other principal U.S. national securities exchange on which the Shares are traded, the Board may take any action under the Plan that the Committee is authorized to take. In the event the Board takes such action references to the Committee hereunder shall be understood to refer to the Board.

**5. OPTIONS**

**5.1. Grant of Options.** Options may be granted hereunder to Participants either alone or in addition to other Awards granted under the Plan. Any Option shall be subject to the terms and conditions of this Article and to such additional terms and conditions, not inconsistent with the provisions of the Plan, as the Committee shall deem desirable.

**5.2. Award Agreements.** All Options granted pursuant to this Article shall be evidenced by a written Award Agreement in such form and containing such terms and conditions as the Committee shall determine which are not inconsistent with the provisions of the Plan. The terms of Options need not be the same with respect to each Participant. Granting an Option pursuant to the Plan shall impose no obligation on the recipient to exercise such Option. Any individual who is granted an Option pursuant to this Article may hold more than one Option granted pursuant to the Plan at the same time.

**5.3. Option Price.** Other than in connection with Substitute Awards, the option price per each Share purchasable under any Option granted pursuant to this Article shall not be less than 100% of the Fair Market Value of one Share on the date of grant of such Option; provided, however, that in the case of an Incentive Stock Option granted to a Participant who, at the time of the grant, owns stock representing more than 10% of the voting power of all classes of stock of the Company or any Affiliate, the option price per share shall be no less than 110% of the Fair Market Value of one Share on the date of grant. Other than pursuant to Section 12.2, the Committee shall not without the approval of the Company's stockholders (a) lower the option price per Share of an Option after it is granted, (b) cancel an Option when the option price per Share exceeds the Fair Market Value of one Share in exchange for cash or another Award (other than in connection with a Change in Control as defined in Section 11.3 or Substitute Awards), and (c) take any other action with respect to an Option that would be treated as a repricing under the rules and regulations of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded).

**5.4. Option Term.** The term of each Option shall be fixed by the Committee in its sole discretion; provided that no Option shall be exercisable after the expiration of ten (10) years from the date the Option is granted, except in the event of death or disability; provided, however, that the term of the Option shall not exceed five (5) years from the date the Option is granted in the case of an Incentive Stock Option granted to a Participant who, at the time of the grant, owns stock representing more than 10% of the voting power of all classes of stock of the Company or any Affiliate.

**5.5. Exercise of Options.**

(a) Vested Options granted under the Plan may be exercised by the Participant or by a Permitted Assignee thereof (or by the Participant's executors, administrators, guardian or legal representative, as may be provided in an Award Agreement) as to all or part of the Shares covered thereby, by the giving of notice of exercise to the Company or its designated agent, specifying the number of Shares to be purchased. The notice of exercise shall be in such form, made in such manner, and shall comply with such other requirements consistent with the provisions of the Plan as the Committee may from time to time prescribe.

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(b) Unless otherwise provided in an Award Agreement, full payment of such purchase price shall be made at the time of exercise and shall be made (i) in cash or cash equivalents (including certified check or bank check or wire transfer of immediately available funds), (ii) by tendering previously acquired Shares (either actually or by attestation), valued at their then Fair Market Value, (iii) with the consent of the Committee, by delivery of other consideration (including, where permitted by law and the Committee, other Awards) having a Fair Market Value on the exercise date equal to the total purchase price, (iv) with the consent of the Committee, by withholding Shares otherwise issuable in connection with the exercise of the Option, (v) through any other method specified in an Award Agreement (including same-day sales through a broker), or (vi) any combination of any of the foregoing. In no event may any Option granted hereunder be exercised for a fraction of a Share. No adjustment shall be made for cash dividends or other rights for which the record date is prior to the date of such issuance.

(c) Notwithstanding the foregoing, an Award Agreement may provide that if on the last day of the term of an Option the Fair Market Value of one Share exceeds the option price per Share, the Participant has not exercised the Option and the Option has not expired, the Option shall be deemed to have been exercised by the Participant on such day with payment made by withholding Shares otherwise issuable in connection with the exercise of the Option. In such event, the Company shall deliver to the Participant the number of Shares for which the Option was deemed exercised, less the number of Shares required to be withheld for the payment of the total purchase price and required withholding taxes; provided, however, any fractional Share shall be settled in cash.

(d) No Option granted to an Employee who is a non-exempt employee for purposes of the Fair Labor Standards Act of 1938, as amended, shall be first exercisable for any Shares until at least six months following the date of grant of the Option. Notwithstanding the foregoing, consistent with the provisions of the Worker Economic Opportunity Act, (i) in the event of the Employee's death or disability, (ii) upon a corporate transaction in which such Option is not assumed, continued, or substituted, (iii) upon a Change in Control, or (iv) upon the Employee's retirement (as such term may be defined in the Employee's Award Agreement or in another applicable agreement or in accordance with the Company's then current employment policies and guidelines), any such vested Options may be exercised earlier than six months following the date of grant. The foregoing provision is intended to operate so that any income derived by a non-exempt employee in connection with the exercise or vesting of an Option will be exempt from his or her regular rate of pay.

**5.6. Form of Settlement.** In its sole discretion, the Committee may provide in the form of Award Agreement that the Shares to be issued upon an Option's exercise shall be in the form of Restricted Stock or other similar securities.

**5.7. Incentive Stock Options.** The Committee may grant Options intended to qualify as incentive stock options as defined in Section 422 of the Code, to any employee of the Company or any Affiliate, subject to the requirements of Section 422 of the Code. Notwithstanding anything in Section 3.1 to the contrary and solely for the purposes of determining whether Shares are available for the grant of incentive stock options under the Plan, the maximum aggregate number of Shares that may be issued pursuant to incentive stock options granted under the Plan shall be 7.0 million Shares, subject to adjustment as provided in Section 12.2.

## **6. STOCK APPRECIATION RIGHTS**

**6.1. Grant and Exercise.** The Committee may provide Stock Appreciation Rights (a) in conjunction with all or part of any Option granted under the Plan or at any subsequent time during the term of such Option, (b) in conjunction with all or part of any Award (other than an Option) granted under the Plan or at any subsequent time during the term of such Award, or (c) without regard to any Option or other Award, in each case upon such terms and conditions as the Committee may establish in its sole discretion.

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**6.2. Terms and Conditions.** Stock Appreciation Rights shall be subject to such terms and conditions, not inconsistent with the provisions of the Plan, as shall be determined from time to time by the Committee, including the following:

(a) Upon the exercise of a Stock Appreciation Right, the holder shall have the right to receive the excess of (i) the Fair Market Value of one Share on the date of exercise (or such amount less than such Fair Market Value as the Committee shall so determine at any time during a specified period before the date of exercise) over (ii) the grant price of the Stock Appreciation Right.

(b) Upon the exercise of a Stock Appreciation Right, the Committee shall determine in its sole discretion whether payment shall be made in cash, in whole Shares or other property, or any combination thereof.

(c) The terms and conditions of Stock Appreciation Rights need not be the same with respect to each recipient.

(d) The Committee may impose such other conditions on the exercise of any Stock Appreciation Right, as it shall deem appropriate. A Stock Appreciation Right shall have (i) a grant price per Share of not less than the Fair Market Value of one Share on the date of grant or, if applicable, on the date of grant of an Option with respect to a Stock Appreciation Right granted in exchange for or in tandem with, but subsequent to, the Option (subject to the requirements of Section 409A of the Code with respect to a Stock Appreciation Right granted in exchange for or in conjunction with, but subsequent to, an Option), except in the case of Substitute Awards or in connection with an adjustment provided in Section 12.2 and (ii) a term not greater than ten (10) years. In addition to the foregoing, but subject to Section 12.2, the Committee shall not without the approval of the Company's stockholders (x) lower the grant price per Share of any Stock Appreciation Right after it is granted, (y) cancel any Stock Appreciation Right when the grant price per Share exceeds the Fair Market Value of the underlying Shares in exchange for cash or another Award (other than in connection with a Change in Control as defined in Section 11.3 or Substitute Awards), and (z) take any other action with respect to any Stock Appreciation Right that would be treated as a repricing under the rules and regulations of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded).

(e) In no event may any Stock Appreciation Right granted hereunder be exercised for a fraction of a Share. No adjustment shall be made for cash dividends or other rights for which the record date is prior to the date of such issuance.

(f) An Award Agreement may provide that if on the last day of the term of a Stock Appreciation Right the Fair Market Value of one Share exceeds the grant price per Share of the Stock Appreciation Right, the Participant has not exercised the Stock Appreciation Right or the tandem Option (if applicable), and neither the Stock Appreciation Right nor the Option has expired, the Stock Appreciation Right shall be deemed to have been exercised by the Participant on such day. In such event, the Company shall make payment to the Participant in accordance with this Section, reduced by the number of Shares (or cash) required for withholding taxes; any fractional Share shall be settled in cash.

(g) No Stock Appreciation Right granted to an Employee who is a non-exempt employee for purposes of the Fair Labor Standards Act of 1938, as amended, shall be first exercisable for any Shares until at least six months following the date of grant of the Stock Appreciation Right. Notwithstanding the foregoing, consistent with the provisions of the Worker Economic Opportunity Act, (i) in the event of the Employee's death or disability, (ii) upon a corporate transaction in which such Stock Appreciation Right is not assumed, continued, or substituted, (iii) upon a Change in Control, or (iv) upon the Employee's retirement (as such term may be defined in the Employee's Award Agreement or in another applicable agreement or in accordance with the Company's then current employment policies and guidelines), any such vested Stock Appreciation Rights may be exercised earlier than six months following the date of grant. The foregoing provision is intended to operate so that any income derived by a non-exempt employee in connection with the exercise or vesting of a Stock Appreciation Right will be exempt from his or her regular rate of pay.

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### **7. RESTRICTED STOCK AWARDS**

**7.1. Grants.** Awards of Restricted Stock may be issued hereunder to Participants either alone or in addition to other Awards granted under the Plan (a Restricted Stock Award ), and such Restricted Stock Awards may also be available as a form of payment of Performance Awards and other earned cash-based incentive compensation. A Restricted Stock Award shall be subject to vesting restrictions imposed by the Committee covering a period of time specified by the Committee. The Committee has absolute discretion to determine whether any consideration (other than services) is to be received by the Company or any Affiliate as a condition precedent to the issuance of Restricted Stock.

**7.2. Award Agreements.** The terms of any Restricted Stock Award granted under the Plan shall be set forth in an Award Agreement which shall contain provisions determined by the Committee and not inconsistent with the Plan. The terms of Restricted Stock Awards need not be the same with respect to each Participant.

**7.3. Rights of Holders of Restricted Stock.** Unless otherwise provided in the Award Agreement, beginning on the date of grant of the Restricted Stock Award and subject to execution of the Award Agreement, the Participant shall become a stockholder of the Company with respect to all Shares subject to the Award Agreement and shall have all of the rights of a stockholder, including the right to vote such Shares and the right to receive distributions made with respect to such Shares; provided, however, that except as otherwise provided in an Award Agreement any Shares or any other property distributed as a dividend or otherwise with respect to any Restricted Stock as to which the restrictions have not yet lapsed shall be subject to the same restrictions as such Restricted Stock.

### **8. RESTRICTED STOCK UNIT AWARDS**

**8.1. Grants.** Other Awards of units having a value equal to an identical number of Shares ( Restricted Stock Unit Awards ) may be granted hereunder to Participants either alone or in addition to other Awards granted under the Plan. Restricted Stock Unit Awards shall also be available as a form of payment of other Awards granted under the Plan and other earned cash-based incentive compensation.

**8.2. Award Agreements.** The terms of Restricted Stock Unit Award granted under the Plan shall be set forth in a written Award Agreement which shall contain provisions determined by the Committee and not inconsistent with the Plan. Restricted Stock Unit Awards shall be subject to vesting restrictions imposed by the Committee covering a period of time specified by the Committee. The terms of such Awards need not be the same with respect to each Participant.

**8.3. Payment.** Except as provided in Article 10 or as may be provided in an Award Agreement, Restricted Stock Unit Awards may be paid in cash, Shares, other property, or any combination thereof, in the sole discretion of the Committee. Restricted Stock Unit Awards may be paid in a lump sum or in installments or, in accordance with procedures established by the Committee, on a deferred basis subject to the requirements of Section 409A of the Code.

### **9. PERFORMANCE AWARDS**

**9.1. Grants.** Performance Awards in the form of Performance Cash, Performance Shares or Performance Units, as determined by the Committee in its sole discretion, may be granted hereunder to Participants, for no consideration or for such minimum consideration as may be required by applicable law, either alone or in addition to other Awards granted under the Plan. The performance goals to be achieved for each Performance Period shall be conclusively determined by the Committee and may be based upon the criteria set forth in Section 10.2.

**9.2. Award Agreements.** The terms of any Performance Award granted under the Plan shall be set forth in an Award Agreement which shall contain provisions determined by the Committee and not inconsistent with the

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Plan, including whether such Awards shall have Dividend Equivalents. The terms of Performance Awards need not be the same with respect to each Participant.

**9.3. Terms and Conditions.** The performance criteria to be achieved during any Performance Period and the length of the Performance Period shall be determined by the Committee upon the grant of each Performance Award; provided, however, that a Performance Period shall not be less than 12 months. The amount of the Award to be distributed shall be conclusively determined by the Committee.

**9.4. Payment.** Except as provided in Article 11 or as may be provided in an Award Agreement, Performance Awards will be distributed only after the end of the relevant Performance Period. Performance Awards may be paid in cash, Shares, other property, or any combination thereof, in the sole discretion of the Committee. Performance Awards may be paid in a lump sum or in installments following the close of the Performance Period or, in accordance with procedures established by the Committee, on a deferred basis subject to the requirements of Section 409A of the Code.

**10. CODE SECTION 162(m) PROVISIONS**

**10.1. Covered Employees.** Notwithstanding any other provision of the Plan, if the Committee determines at the time a Restricted Stock Award, a Performance Award or an Restricted Stock Unit Award is granted to a Participant who is, or is likely to be, as of the end of the tax year in which the Company would claim a tax deduction in connection with such Award, a Covered Employee, then the Committee may provide that this Article 10 is applicable to such Award.

**10.2. Performance Criteria.** If the Committee determines that a Restricted Stock Award, a Performance Award or an Restricted Stock Unit Award is intended to be subject to this Article 10, the lapsing of restrictions thereon and the distribution of cash, Shares or other property pursuant thereto, as applicable, shall be subject to the achievement of one or more objective performance goals established by the Committee, which shall be based on the attainment of specified levels of one or any combination of the following: net sales; revenue; revenue or product revenue growth; operating income or loss (before or after taxes); pre- or after-tax income or loss (before or after allocation of corporate overhead and bonus); net earnings or loss; earnings or loss per share; net income or loss (before or after taxes); return on equity; total stockholder return; return on assets or net assets; attainment of strategic and operational initiatives; appreciation in and/or maintenance of the price of the Shares or any other publicly-traded securities of the Company; market share; gross profits; earnings or losses (including earnings or losses before taxes, earnings or losses before interest and taxes, earnings or losses before interest, taxes and depreciation or earnings or losses before interest, taxes, depreciation and amortization); economic value-added models (or equivalent metrics); comparisons with various stock market indices; reductions in costs; cash flow or cash flow per share (before or after dividends); return on capital (including return on total capital or return on invested capital); cash flow return on investment; improvement in or attainment of expense levels or working capital levels; operating margin; gross margin; year-end cash; cash margin; debt reduction; stockholder's equity; market share; achievement of drug development milestones; regulatory achievements including approval of a compound; progress of internal research or clinical programs; progress of partnered programs; implementation or completion of projects and processes; partner satisfaction; budget management; clinical achievements; completing phases of a clinical study (including the treatment phase); or announcing or presenting preliminary or final data from clinical studies; in each case, whether on particular timelines or generally); timely completion of clinical trials; submission of INDs and NDAs and other regulatory achievements; partner or collaborator achievements; internal controls, including those related to the Sarbanes-Oxley Act of 2002; research progress, including the development of programs; financing; investor relation, analysts and communication; manufacturing achievements (including obtaining particular yields from manufacturing runs and other measurable objectives related to process development activities); strategic partnerships or transactions (including in-licensing and out-licensing of intellectual property; establishing relationships with commercial entities with respect to the marketing, distribution and sale of the Company's products (including with group purchasing organizations, distributors and other vendors); supply chain achievements (including establishing relationships with

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manufacturers or suppliers of active pharmaceutical ingredients and other component materials and manufacturers of the Company's products); co-development, co-marketing, profit sharing, joint venture or other similar arrangements; financing and other capital raising transactions (including sales of the Company's equity or debt securities); factoring transactions; sales or licenses of the Company's assets, including its intellectual property (whether in a particular jurisdiction or territory or globally or through partnering transactions); implementation, completion or attainment of measurable objectives with respect to research, development, manufacturing, commercialization, products or projects, production volume levels, acquisitions and divestitures; factoring transactions; and recruiting and maintaining personnel. Such performance goals also may be based solely by reference to the Company's performance or the performance of an Affiliate, division, business segment or business unit of the Company, or based upon the relative performance of other companies or upon comparisons of any of the indicators of performance relative to other companies. The Committee may also exclude charges related to an event or occurrence which the Committee determines should appropriately be excluded, including (a) restructurings, discontinued operations, extraordinary items, and other unusual or non-recurring charges, (b) an event either not directly related to the operations of the Company or not within the reasonable control of the Company's management, or (c) the cumulative effects of tax or accounting changes in accordance with U.S. generally accepted accounting principles. Such performance goals shall be set by the Committee within the time period prescribed by, and shall otherwise comply with the requirements of, Section 162(m) of the Code, and the regulations thereunder.

**10.3. Adjustments.** Notwithstanding any provision of the Plan (other than Article 11), with respect to any Restricted Stock, Performance Award or Restricted Stock Unit Award that is subject to this Section 10, the Committee may adjust downwards, but not upwards, the amount payable pursuant to such Award, and the Committee may not waive the achievement of the applicable performance goals, except in the case of the death or disability of the Participant or as otherwise determined by the Committee in special circumstances.

**10.4. Restrictions.** The Committee shall have the power to impose such other restrictions on Awards subject to this Article as it may deem necessary or appropriate to ensure that such Awards satisfy all requirements for performance-based compensation within the meaning of Section 162(m) of the Code.

**10.5. Limitations on Grants to Individual Participants.** Subject to adjustment as provided in Section 12.2, no Participant may be granted (i) Options or Stock Appreciation Rights during any 36-month period with respect to more than 2,000,000 Shares or (ii) Restricted Stock, Performance Awards and/or Restricted Stock Unit Awards that are denominated in Shares in any 36-month period with respect to more than 1,000,000 Shares that are intended to comply with the performance-based exception under Code Section 162(m) (collectively, the Limitations). In addition to the foregoing, the maximum dollar value that may be granted to any Participant for each 12 months in a Performance Period with respect to Performance Awards that are intended to comply with the performance-based exception under Code Section 162(m) and are denominated in cash is \$5,000,000. If an Award is cancelled, the cancelled Award shall continue to be counted toward the applicable Limitations (or, in the case of a performance award denominated in cash, to be counted toward the dollar amount in the preceding sentence).

**11. CHANGE IN CONTROL PROVISIONS**

**11.1. Impact on Certain Awards.** The Committee, in its discretion, may determine that in the event of a Change in Control of the Company (as defined in Section 11.3) Options and Stock Appreciation Rights outstanding as of the date of the Change in Control shall be cancelled and terminated without payment therefor if the Fair Market Value of one Share as of the date of the Change in Control is less than the Option per Share option price or Stock Appreciation Right per Share grant price.

**11.2. Assumption or Substitution of Certain Awards.**

(a) To the extent provided in an Award Agreement, in the event of a Change in Control of the Company in which the successor company assumes or substitutes for an Option, Stock Appreciation Right,

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Restricted Stock Award or Restricted Stock Unit Award (or in which the Company is the ultimate parent corporation and continues the Award), if a Participant's employment with such successor company (or the Company) or a subsidiary thereof terminates within the time period following such Change in Control set forth in the Award Agreement (or prior thereto if applicable) and under the circumstances specified in the Award Agreement: (i) Options and Stock Appreciation Rights outstanding as of the date of such termination of employment will immediately vest, become fully exercisable, and may thereafter be exercised for the period of time set forth in the Award Agreement, (ii) the restrictions, limitations and other conditions applicable to Restricted Stock shall lapse and the Restricted Stock shall become free of all restrictions, limitations and conditions and become fully vested, and (iii) the restrictions, limitations and other conditions applicable to any Restricted Stock Unit Awards or any other Awards shall lapse, and such Restricted Stock Unit Awards or such other Awards shall become free of all restrictions, limitations and conditions and become fully vested and transferable to the full extent of the original grant. For the purposes of this Section, an Option, Stock Appreciation Right, Restricted Stock Award or Restricted Stock Unit Award shall be considered assumed or substituted for if following the Change in Control the Award confers the right to purchase or receive, for each Share subject to the Option, Stock Appreciation Right, Restricted Stock Award or Restricted Stock Unit Award immediately prior to the Change in Control, the consideration (whether stock, cash or other securities or property) received in the transaction constituting a Change in Control by holders of Shares for each Share held on the effective date of such transaction (and if holders were offered a choice of consideration, the type of consideration chosen by the holders of a majority of the outstanding shares); provided, however, that if such consideration received in the transaction constituting a Change in Control is not solely common stock of the successor company, the Committee may, with the consent of the successor company, provide that the consideration to be received upon the exercise or vesting of an Option, Stock Appreciation Right, Restricted Stock Award or Restricted Stock Unit Award, for each Share subject thereto, will be solely common stock of the successor company substantially equal in fair market value to the per Share consideration received by holders of Shares in the transaction constituting a Change in Control. The determination of such substantial equality of value of consideration shall be made by the Committee in its sole discretion and its determination shall be conclusive and binding.

(b) Unless otherwise provided in an Award Agreement, in the event of a Change in Control of the Company, to the extent that the successor company does not assume or substitute for an Option, Stock Appreciation Right, Restricted Stock Award, Restricted Stock Unit Award or Performance Award (or in which the Company is the ultimate parent corporation and continues the Award), then immediately prior to the Change in Control: (i) those Options and Stock Appreciation Rights outstanding as of the date of the Change in Control that are not assumed or substituted for (or continued) shall immediately vest and become fully exercisable, (ii) restrictions, limitations and conditions on Restricted Stock not assumed or substituted for (or continued) shall lapse and the Restricted Stock shall become free of all restrictions, limitations and conditions and become fully vested, (iii) the restrictions limitations and conditions applicable to any Restricted Stock Unit Awards or any other Awards not assumed or substituted for (or continued) shall lapse, and such Restricted Stock Unit Awards or such other Awards shall become free of all restrictions, limitations and conditions and become fully vested and transferable to the full extent of the original grant, (iv) all Performance Awards not assumed or substituted for (or continued) shall be considered to be earned and payable in full, and any deferral or other restriction shall lapse and such Performance Awards shall be immediately settled or distributed, and (v) all Awards not assumed or substituted for (or continued) shall terminate immediately after the Change in Control.

(c) The Committee, in its discretion, may determine that, upon the occurrence of a Change in Control of the Company, each Option and Stock Appreciation Right outstanding shall terminate within a specified number of days after notice to the Participant, and/or that each Participant shall receive, with respect to each Share subject to such Option or Stock Appreciation Right, an amount equal to the excess (if any) of the Fair Market Value of such Share immediately prior to the occurrence of such Change in Control over the exercise price per Share of such Option and/or Stock Appreciation Right; such amount to be payable in cash, in one or more kinds of stock or property (including the stock or property, if any, payable in the transaction) or in a combination thereof, as the Committee, in its discretion, shall determine.



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**11.3. Change in Control.** For purposes of the Plan, unless otherwise provided in an Award Agreement, Change in Control means the occurrence of any one of the following events:

- (i) During any twenty-four (24) month period, individuals who, as of the beginning of such period, constitute the Board (the Incumbent Directors ) cease for any reason to constitute at least a majority of the Board, provided that any person becoming a director subsequent to the beginning of such period whose election or nomination for election was approved by a vote of at least a majority of the Incumbent Directors then on the Board (either by a specific vote or by approval of the proxy statement of the Company in which such person is named as a nominee for director, without written objection to such nomination) shall be an Incumbent Director; provided, however, that no individual initially elected or nominated as a director of the Company as a result of an actual or threatened election contest with respect to directors or as a result of any other actual or threatened solicitation of proxies by or on behalf of any person other than the Board shall be deemed to be an Incumbent Director;
- (ii) Any person (as such term is defined in the Exchange Act and as used in Sections 13(d)(3) and 14(d)(2) of the Exchange Act) is or becomes a beneficial owner (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 50% or more of the combined voting power of the Company's then outstanding securities eligible to vote for the election of the Board (the Company Voting Securities ); provided, however, that the event described in this paragraph (ii) shall not be deemed to be a Change in Control by virtue of any of the following acquisitions: (A) by the Company or any Affiliate, (B) by any employee benefit plan (or related trust) sponsored or maintained by the Company or any Affiliate, (C) by any underwriter temporarily holding securities pursuant to an offering of such securities, (D) pursuant to a Non-Qualifying Transaction, as defined in paragraph (iii), or (E) by any person of Voting Securities from the Company, if a majority of the Incumbent Board approves in advance the acquisition of beneficial ownership of 50% or more of Company Voting Securities by such person;
- (iii) The consummation of a merger, consolidation, statutory share exchange or similar form of corporate transaction involving the Company or any of its Affiliates that requires the approval of the Company's stockholders, whether for such transaction or the issuance of securities in the transaction (a Business Combination ), unless immediately following such Business Combination: (A) more than 60% of the total voting power of (x) the corporation resulting from such Business Combination (the Surviving Corporation ), or (y) if applicable, the ultimate parent corporation that directly or indirectly has beneficial ownership of 100% of the voting securities eligible to elect directors of the Surviving Corporation (the Parent Corporation ), is represented by Company Voting Securities that were outstanding immediately prior to such Business Combination (or, if applicable, is represented by shares into which such Company Voting Securities were converted pursuant to such Business Combination), and such voting power among the holders thereof is in substantially the same proportion as the voting power of such Company Voting Securities among the holders thereof immediately prior to the Business Combination, (B) no person (other than any employee benefit plan (or related trust) sponsored or maintained by the Surviving Corporation or the Parent Corporation), is or becomes the beneficial owner, directly or indirectly, of 50% or more of the total voting power of the outstanding voting securities eligible to elect directors of the Parent Corporation (or, if there is no Parent Corporation, the Surviving Corporation) and (C) at least a majority of the members of the board of directors of the Parent Corporation (or, if there is no Parent Corporation, the Surviving Corporation) following the consummation of the Business Combination were Incumbent Directors at the time of the Board's approval of the execution of the initial agreement providing for such Business Combination (any Business Combination which satisfies all of the criteria specified in (A), (B) and (C) above shall be deemed to be a Non-Qualifying Transaction );
- (iv) The stockholders of the Company approve a plan of complete liquidation or dissolution of the Company or the consummation of a sale of all or substantially all of the Company's assets; or
- (v) The occurrence of any other event that the Board determines by a duly approved resolution constitutes a Change in Control.

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Notwithstanding the foregoing, a Change in Control shall not be deemed to occur solely because any person acquires beneficial ownership of more than 50% of the Company Voting Securities as a result of the acquisition of Company Voting Securities by the Company which reduces the number of Company Voting Securities outstanding; provided, that if after such acquisition by the Company such person becomes the beneficial owner of additional Company Voting Securities that increases the percentage of outstanding Company Voting Securities beneficially owned by such person, a Change in Control of the Company shall then occur.

**12. GENERALLY APPLICABLE PROVISIONS**

**12.1. *Amendment and Termination of the Plan.*** The Board may, from time to time, alter, amend, suspend or terminate the Plan as it shall deem advisable, subject to any requirement for stockholder approval imposed by applicable law, including the rules and regulations of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded); provided that the Board may not amend the Plan in any manner that would result in noncompliance with Rule 16b-3 of the Exchange Act; and further provided that the Board may not, without the approval of the Company's stockholders to the extent required by such applicable law, amend the Plan to (a) increase the number of Shares that may be the subject of Awards under the Plan (except for adjustments pursuant to Section 12.2); (b) expand the types of awards available under the Plan; (c) materially expand the class of persons eligible to participate in the Plan; (d) amend any provision of Section 5.3 or the last sentence of Section 6.2(d); or (e) increase the maximum permissible term of any Option specified by Section 5.4 or the maximum permissible term of a Stock Appreciation Right specified by Section 6.2(d). The Board may not without the approval of the Company's stockholders cancel an Option or Stock Appreciation Right in exchange for cash or take any action with respect to an Option or Stock Appreciation Right that may be treated as a repricing under the rules and regulations of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Shares are traded), including a reduction of the exercise price of an Option or the grant price of a Stock Appreciation Right or the exchange of an Option or Stock Appreciation Right for cash or another Award. In addition, no amendments to, or termination of, the Plan shall in any way impair the rights of a Participant under any Award previously granted without such Participant's consent.

**12.2. *Adjustments.*** In the event of any merger, reorganization, consolidation, recapitalization, dividend or distribution (whether in cash, shares or other property, other than a regular cash dividend), stock split, reverse stock split, spin-off or similar transaction or other change in corporate structure affecting the Shares or the value thereof, such adjustments and other substitutions shall be made to the Plan and to Awards as the Committee deems equitable or appropriate taking into consideration the accounting and tax consequences, including such adjustments in the aggregate number, class and kind of securities that may be delivered under the Plan, the Limitations, the maximum number of Shares that may be issued pursuant to Incentive Stock Options and, in the aggregate or to any one Participant, in the number, class, kind and option or exercise price of securities subject to outstanding Awards granted under the Plan (including, if the Committee deems appropriate, the substitution of similar options to purchase the shares of, or other awards denominated in the shares of, another company) as the Committee may determine to be appropriate in its sole discretion; provided, however, that the number of Shares subject to any Award shall always be a whole number.

**12.3. *Transferability of Awards.*** Except as provided below, no Award and no Shares subject to Awards described in Article 8 that have not been issued or as to which any applicable restriction, performance or deferral period has not lapsed, may be sold, assigned, transferred, pledged or otherwise encumbered, other than by will or the laws of descent and distribution, and such Award may be exercised during the life of the Participant only by the Participant or the Participant's guardian or legal representative. To the extent and under such terms and conditions as determined by the Committee, a Participant may assign or transfer an Award (each transferee thereof, a Permitted Assignee) to a family member as such term is defined in the General Instructions to Form S-8 (whether by gift or a domestic relations order); provided that such Permitted Assignee shall be bound by and subject to all of the terms and conditions of the Plan and the Award Agreement relating to the transferred Award and shall execute an agreement satisfactory to the Company evidencing such obligations; and provided

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further that such Participant shall remain bound by the terms and conditions of the Plan. The Company shall cooperate with any Permitted Assignee and the Company's transfer agent in effectuating any transfer permitted under this Section.

**12.4. Termination of Employment.** The Committee shall determine and set forth in each Award Agreement whether any Awards granted in such Award Agreement will continue to be exercisable, continue to vest or be earned and the terms of such exercise, vesting or earning, on and after the date that a Participant ceases to be employed by or to provide services to the Company or any Affiliate (including as a Director), whether by reason of death, disability, voluntary or involuntary termination of employment or services, or otherwise. The date of termination of a Participant's employment or services will be determined by the Committee, which determination will be final.

**12.5. Deferral; Dividend Equivalents.** The Committee shall be authorized to establish procedures pursuant to which the payment of any Award may be deferred. Subject to the provisions of the Plan and any Award Agreement, the recipient of an Award (including any deferred Award) other than an Option or Stock Appreciation Right may, if so determined by the Committee, be entitled to receive, currently or on a deferred basis, cash, stock or other property dividends, or cash payments in amounts equivalent to cash, stock or other property dividends on Shares ( Dividend Equivalents ) with respect to the number of Shares covered by the Award, as determined by the Committee, in its sole discretion. The Committee may provide that such amounts and Dividend Equivalents (if any) shall be deemed to have been reinvested in additional Shares or otherwise reinvested and may provide that such amounts and Dividend Equivalents are subject to the same vesting or performance conditions as the underlying Award.

**13. MISCELLANEOUS**

**13.1. Tax Withholding.** The Company shall have the right to make all payments or distributions pursuant to the Plan to a Participant (or a Permitted Assignee thereof) (any such person, a Payee ) net of any applicable federal, state and local taxes required to be paid or withheld as a result of (a) the grant of any Award, (b) the exercise of an Option or Stock Appreciation Right, (c) the delivery of Shares or cash, (d) the lapse of any restrictions in connection with any Award or (e) any other event occurring pursuant to the Plan. The Company or any Affiliate shall have the right to withhold from wages or other amounts otherwise payable to such Payee such withholding taxes as may be required by law, or to otherwise require the Payee to pay such withholding taxes. If the Payee shall fail to make such tax payments as are required, the Company or its Affiliates shall, to the extent permitted by law, have the right to deduct any such taxes from any payment of any kind otherwise due to such Payee or to take such other action as may be necessary to satisfy such withholding obligations. The Committee shall be authorized to establish procedures for election by Participants to satisfy such obligation for the payment of such taxes by tendering previously acquired Shares (either actually or by attestation, valued at their then Fair Market Value), or by directing the Company to retain Shares (up to the Participant's minimum required tax withholding rate or such other rate that will not cause an adverse accounting consequence or cost) otherwise deliverable in connection with the Award.

**13.2. Right of Discharge Reserved; Claims to Awards.** Nothing in the Plan nor the grant of an Award hereunder shall confer upon any Employee, Director or Consultant the right to continue in the employment or service of the Company or any Affiliate or affect any right that the Company or any Affiliate may have to terminate the employment or service of (or to demote or to exclude from future Awards under the Plan) any such Employee, Director or Consultant at any time for any reason. Except as specifically provided by the Committee, the Company shall not be liable for the loss of existing or potential profit from an Award granted in the event of termination of an employment or other relationship. No Employee, Director or Consultant shall have any claim to be granted any Award under the Plan, and there is no obligation for uniformity of treatment of Employees, Directors or Consultants under the Plan.

**13.3. Prospective Recipient.** The prospective recipient of any Award under the Plan shall not, with respect to such Award, be deemed to have become a Participant, or to have any rights with respect to such Award, until and

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unless such recipient shall have executed an agreement or other instrument evidencing the Award and delivered a copy thereof to the Company, and otherwise complied with the then applicable terms and conditions.

**13.4. *Substitute Awards.*** Notwithstanding any other provision of the Plan, the terms of Substitute Awards may vary from the terms set forth in the Plan to the extent the Committee deems appropriate to conform, in whole or in part, to the provisions of the awards in substitution for which they are granted.

**13.5. *Cancellation of Award.***

(a) Notwithstanding anything to the contrary contained herein, an Award Agreement may provide that the Award shall be canceled if the Participant, without the consent of the Company, while employed by, or providing services to, the Company or any Affiliate or after termination of such employment or services, establishes a relationship with a competitor of the Company or any Affiliate or engages in activity that is in conflict with or adverse to the interest of the Company or any Affiliate (including conduct contributing to any financial restatements or financial irregularities), as determined by the Committee in its sole discretion. The Committee may provide in an Award Agreement that if within the time period specified in the Agreement the Participant establishes a relationship with a competitor or engages in an activity referred to in the preceding sentence, the Participant will forfeit any gain realized on the vesting or exercise of the Award and must repay such gain to the Company.

(b) In the event the Participant ceases to be employed by, or provide services to, the Company on account of a termination for cause (as defined below) by the Company, any Award held by the Participant shall terminate as of the date the Participant ceases to be employed by, or provide services to, the Company. In addition, notwithstanding any other provisions of this Section, if the Committee determines that the Participant has engaged in conduct that constitutes cause at any time while the Participant is employed by, or providing services to, the Company or after the Participant's termination of employment or services, any Awards held by the Participant shall immediately terminate. In the event a Participant's employment or services is terminated for cause, in addition to the immediate termination of all Awards, the Participant shall automatically forfeit all shares underlying any exercised portion of an Option for which the Company has not yet delivered the share certificates, upon refund by the Company of the option price paid by the Participant for such shares.

(c) For purposes of this Section, cause shall mean, unless otherwise provided in an Award Agreement or another agreement between the Participant and the Company or an Affiliate or a plan maintained by the Company or an Affiliate in which the Participant participates, a determination by the Committee that the Participant has breached his or her employment or service contract with the Company, or has been engaged in disloyalty to the Company, including, without limitation, fraud, embezzlement, theft, commission of a felony or proven dishonesty in the course of his or her employment or service, or has disclosed trade secrets or confidential information of the Company to persons not entitled to receive such information, or has breached any written noncompetition or nonsolicitation agreement between the Participant and the Company or has engaged in such other behavior detrimental to the interests of the Company as the Committee determines.

**13.6. *Stop Transfer Orders.*** All certificates for Shares delivered under the Plan pursuant to any Award shall be subject to such stop-transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Shares are then listed, and any applicable federal or state securities law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

**13.7. *Nature of Payments.*** All Awards made pursuant to the Plan are in consideration of services performed or to be performed for the Company or any Affiliate, division or business unit of the Company. Any income or gain realized pursuant to Awards under the Plan constitutes a special incentive payment to the Participant and shall not be taken into account, to the extent permissible under applicable law, as compensation for purposes of

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any of the employee benefit plans of the Company or any Affiliate except as may be determined by the Committee or by the Board or board of directors of the applicable Affiliate.

**13.8. *Other Plans.*** Nothing contained in the Plan shall prevent the Board from adopting other or additional compensation arrangements, subject to stockholder approval if such approval is required; and such arrangements may be either generally applicable or applicable only in specific cases.

**13.9. *Severability.*** The provisions of the Plan shall be deemed severable. If any provision of the Plan shall be held unlawful or otherwise invalid or unenforceable in whole or in part by a court of competent jurisdiction or by reason of a change in a law or regulation, such provision shall (a) be deemed limited to the extent that such court of competent jurisdiction deems it lawful, valid and/or enforceable and as so limited shall remain in full force and effect, and (b) not affect any other provision of the Plan or part thereof, each of which shall remain in full force and effect. If the making of any payment or the provision of any other benefit required under the Plan shall be held unlawful or otherwise invalid or unenforceable by a court of competent jurisdiction, such unlawfulness, invalidity or unenforceability shall not prevent any other payment or benefit from being made or provided under the Plan, and if the making of any payment in full or the provision of any other benefit required under the Plan in full would be unlawful or otherwise invalid or unenforceable, then such unlawfulness, invalidity or unenforceability shall not prevent such payment or benefit from being made or provided in part, to the extent that it would not be unlawful, invalid or unenforceable, and the maximum payment or benefit that would not be unlawful, invalid or unenforceable shall be made or provided under the Plan.

**13.10. *Construction.*** As used in the Plan, the words *include* and *including*, and variations thereof, shall not be deemed to be terms of limitation, but rather shall be deemed to be followed by the words *without limitation*.

**13.11. *Unfunded Status of the Plan.*** The Plan is intended to constitute an unfunded plan for incentive and deferred compensation. With respect to any payments not yet made to a Participant by the Company, nothing contained herein shall give any such Participant any rights that are greater than those of a general creditor of the Company. In its sole discretion, the Committee may authorize the creation of trusts or other arrangements to meet the obligations created under the Plan to deliver the Shares or payments in lieu of or with respect to Awards hereunder; provided, however, that the existence of such trusts or other arrangements is consistent with the unfunded status of the Plan.

**13.12. *Governing Law.*** The Plan and all determinations made and actions taken thereunder, to the extent not otherwise governed by the Code or the laws of the United States, shall be governed by the laws of the State of Delaware, without reference to principles of conflict of laws, and construed accordingly.

**13.13. *Effective Date of Plan; Termination of Plan.*** The Plan shall be effective on the date of the approval of the Plan by the holders of the shares entitled to vote at a duly constituted meeting of the stockholders of the Company. The Plan shall be null and void and of no effect if the foregoing condition is not fulfilled and in such event each Award shall, notwithstanding any of the preceding provisions of the Plan, be null and void and of no effect. Awards may be granted under the Plan at any time and from time to time on or prior to the tenth anniversary of the effective date of the Plan, on which date the Plan will expire except as to Awards then outstanding under the Plan. Such outstanding Awards shall remain in effect until they have been exercised or terminated, or have expired.

**13.14. *Foreign Employees and Consultants.*** Awards may be granted to Participants who are foreign nationals or employed or providing services outside the United States, or both, on such terms and conditions different from those applicable to Awards to Employees employed or providing services in the United States as may, in the judgment of the Committee, be necessary or desirable in order to recognize differences in local law or tax policy. The Committee also may impose conditions on the exercise or vesting of Awards in order to minimize the Company's obligation with respect to tax equalization for Employees or Consultants on assignments outside their home country.

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**13.15. *Compliance with Section 409A of the Code.*** This Plan is intended to comply and shall be administered in a manner that is intended to comply with Section 409A of the Code and shall be construed and interpreted in accordance with such intent. To the extent that an Award or the payment, settlement or deferral thereof is subject to Section 409A of the Code, the Award shall be granted, paid, settled or deferred in a manner that will comply with Section 409A of the Code, including regulations or other guidance issued with respect thereto, except as otherwise determined by the Committee. Any provision of this Plan that would cause the grant of an Award or the payment, settlement or deferral thereof to fail to satisfy Section 409A of the Code shall be amended to comply with Section 409A of the Code on a timely basis, which may be made on a retroactive basis, in accordance with regulations and other guidance issued under Section 409A of the Code.

**13.16. *Captions.*** The captions in the Plan are for convenience of reference only, and are not intended to narrow, limit or affect the substance or interpretation of the provisions contained herein.

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**APPENDIX B**

**ARENA PHARMACEUTICALS, INC.**

**2009 EMPLOYEE STOCK PURCHASE PLAN**

**1. Purpose.** The purpose of the Plan is to provide employees of Arena Pharmaceuticals, Inc. (the Company) and its Designated Subsidiaries with an opportunity to purchase Common Stock of the Company through accumulated payroll deductions. It is the intention of the Company to have the Plan qualify as an Employee Stock Purchase Plan under Section 423 of the Internal Revenue Code of 1986, as amended. The provisions of the Plan, accordingly, shall be construed so as to extend and limit participation in a manner consistent with the requirements of that section of the Code.

After the effective date of the Plan, (i) no new Offering Periods shall commence under the Prior Plan and (ii) all Offering Periods existing under the Prior Plan on the effective date of the Plan are intended to continue in effect under the Plan in accordance with the terms of the Prior Plan.

**2. Definitions.**

- (a) Authorization Form shall mean a form established by the Plan Administrator authorizing payroll deductions, as set forth in Section 4, and containing such other terms and conditions as the Company from time to time may determine.
- (b) Board shall mean the Board of Directors of the Company.
- (c) Code shall mean the Internal Revenue Code of 1986, as amended. References to specific sections of the Code shall be taken to be references to corresponding sections of any successor statute.
- (d) Committee shall mean the committee of members of the Board designated as the Committee in Section 14.
- (e) Common Stock shall mean the common stock of the Company.
- (f) Company shall mean Arena Pharmaceuticals, Inc., or any successor by merger or otherwise, and any Designated Subsidiary of the Company.
- (g) Compensation shall mean all base gross earnings, commissions, overtime, and shift premium before giving effect to any compensation reductions made in connection with plans described in section 401(k) or 125 of the Code, but exclusive of payments for any other compensation.
- (h) Designated Subsidiary shall mean any Subsidiary that has been designated by the Board from time to time in its sole discretion as eligible to participate in the Plan. For purposes of the Plan, BRL Screening, Inc. shall be deemed to have been designated by the Board as a Designated Subsidiary.
- (i) Employee shall mean any individual who is an Employee of the Company for tax purposes whose customary employment with the Company is at least twenty (20) hours per week. For purposes of the Plan, the employment relationship shall be treated as continuing intact while the individual is on sick leave or other leave of absence approved by the Company. Where the period of leave exceeds 90 days and the individual's right to reemployment is not guaranteed either by statute or by contract, the employment relationship shall be deemed to have terminated on the 91st day of such leave.
- (j) Enrollment Date shall mean the first Trading Day of each Offering Period.
- (k) Exercise Date shall mean the last Trading Day of each Purchase Period.

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(l) Fair Market Value shall mean, as of any date, the value of Common Stock determined as follows:

(1) The per share closing price of the Common Stock as reported on the NASDAQ Stock Market on that date (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported);

(2) If the Common Stock is not then listed on the NASDAQ Stock Market, the per share closing price of the Common Stock on such other principal U.S. national securities exchange on which the Common Stock is listed (or if there was no reported closing price on such date, on the last preceding date on which the closing price was reported);

(3) If the Common Stock is not listed on any U.S. national securities exchange but is quoted in an inter-dealer quotation system on a last sale basis, the final ask price of the Common Stock reported on such date (or, if there is no such sale on such date, then on the last preceding date on which a sale was reported); or

(4) If the Common Stock is neither listed on a U.S. national securities exchange nor quoted on an inter-dealer quotation system on a last sale basis, the Fair Market Value shall be determined by the Committee in its sole discretion using appropriate criteria.

(m) Offering Periods shall mean the periods established pursuant to Section 4.

(n) Plan shall mean this 2009 Employee Stock Purchase Plan, as amended from time to time.

(o) Plan Administrator shall mean the Company acting through its authorized officers.

(p) Prior Plan shall mean the Company's 2001 Arena Employee Stock Purchase Plan, as amended.

(q) Purchase Period shall mean, except as otherwise determined by the Committee, the three (3) month period commencing on the next Trading Day following the preceding Exercise Date and ending with the next Exercise Date, except that the first Purchase Period of any Offering Period shall commence on the Enrollment Date and end with the next Exercise Date.

(r) Purchase Price shall mean 85% of the Fair Market Value of a share of Common Stock on the Enrollment Date or on the Exercise Date, whichever is lower; provided however, that the Purchase Price may be adjusted by the Board pursuant to Section 20.

(s) Reserves shall mean the number of shares of Common Stock covered by each option under the Plan that have not yet been exercised and the number of shares of Common Stock which have been authorized for issuance under the Plan but not yet placed under option.

(t) Subsidiary shall mean a corporation, domestic or foreign, of which not less than 50% of the voting shares are held by the Company or a Subsidiary, whether or not such corporation now exists or is hereafter organized or acquired by the Company or a Subsidiary.

(u) Trading Day shall mean a day on which the NASDAQ Stock Market (or such other principal U.S. national securities exchange Common Stock is listed) is open for trading.

**3. Eligibility.**

(a) All Employees who are employed by the Company at least one (1) day before a given Enrollment Date shall be eligible to participate in the Plan.

(b) Any provisions of the Plan to the contrary notwithstanding, no Employee shall be granted an option under the Plan (i) to the extent that, immediately after the grant, such Employee (or any other person whose stock



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would be attributed to such Employee pursuant to Section 424(d) of the Code) would own capital stock of the Company and/or hold outstanding options to purchase such stock possessing five percent (5%) or more of the total combined voting power or value of all classes of the capital stock of the Company or of any parent or subsidiary corporation, or (ii) to the extent that his or her rights to purchase stock under all employee stock purchase plans of the Company and any parent or subsidiary corporation accrues at a rate which exceeds Twenty-Five Thousand Dollars (\$25,000) worth of stock (determined at the fair market value of the shares at the time such option is granted) for each calendar year in which such option is outstanding at any time.

### **4. Offering Periods.**

(a) *Plan Implementation.* The Plan shall be implemented by consecutive, overlapping Offering Periods with a new Offering Period commencing on the first Trading Day on or after January 1, April 1, July 1, and October 1 of each year, or on such other date as the Board or the Committee shall determine, and continuing thereafter until terminated in accordance with Section 20 hereof. All Offering Periods existing under the Prior Plan on the effective date of the Plan shall continue in effect under the Plan, but in accordance with the terms of the Prior Plan, including with respect to their Purchase Price and duration. The shares reserved for issuance under the Plan are available for purchase with respect to Offering Periods existing under the Prior Plan on the effective date of the Plan and those commencing at any time under the Plan. The first new Offering Period under the Plan shall begin on July 1, 2009 and, except as may be otherwise provided for in Section 4(c), shall end on the last Trading Day on or before June 30, 2011.

(b) *Offering Period Duration.* Each Offering Period shall be for a period of twenty-four (24) months during which an option granted pursuant to the Plan may be exercised.

(c) *Automatic Transfer to Lower Price Offering Period.* To the extent permitted by any applicable laws, regulations, rules of the NASDAQ Stock Market (or such other principal U.S. national securities exchange on which the Common Stock is listed), if the Fair Market Value of the Common Stock on any Exercise Date in an Offering Period is lower than the Fair Market Value of the Common Stock on the Enrollment Date of such Offering Period, then all participants in such Offering Period shall be automatically withdrawn from such Offering Period immediately after the exercise of their option on such Exercise Date and automatically re-enrolled in the immediately following Offering Period as of the first day thereof.

(d) *Changes in Offering Period.* The Board or the Committee shall have the power to change the duration of Offering Periods (including the commencement dates thereof) with respect to future offerings without stockholder approval if notice of such change is announced to Employees prior to the scheduled beginning of the first Offering Period to be affected thereafter.

### **5. Participation.**

(a) An Employee may become a participant in the Plan by completing an Authorization Form and filing it with the Plan Administrator prior to the applicable Enrollment Date.

(b) Payroll deductions for a participant shall commence on the first payroll following the Enrollment Date and shall end on the last payroll in the Offering Period to which such authorization is applicable, unless sooner terminated by the participant as provided in Section 10 hereof.

### **6. Payroll Deductions.**

(a) At the time a participant files his or her Authorization Form, he or she shall elect to have payroll deductions made on each payday during the Offering Period in an amount not exceeding fifteen percent (15%) of the Compensation which he or she receives on each pay day during the Offering Period (or such other percentage as may be established by the Board or the Committee from time to time in its sole discretion).

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(b) All payroll deductions made for a participant shall be credited to his or her account under the Plan and shall be withheld in whole percentages only. A participant may not make any additional payments into such account.

(c) A participant may discontinue his or her participation in the Plan as provided in Section 10 hereof, or may increase or decrease the rate of his or her payroll deductions during the Offering Period by filing with the Plan Administrator a new Authorization Form authorizing a change in payroll deduction rate. The Board or the Committee may, in its discretion, limit the number of participation rate changes during any Offering Period. Any such reduction or increase would be effective beginning with the first Purchase Period that begins no earlier than 5 business days after the Plan Administrator's receipt of a new Authorization Form from the participant, unless otherwise determined by the Plan Administrator. A participant's Authorization Form shall remain in effect for successive Offering Periods unless terminated as provided in Section 10 hereof.

(d) Notwithstanding the foregoing, to the extent necessary to comply with Section 423(b)(8) of the Code and Section 3(b) hereof, a participant's payroll deductions may be decreased to zero percent (0%) at any time during a Purchase Period. Payroll deductions shall recommence at the rate provided in such participant's Authorization Form at the beginning of the first Purchase Period that is scheduled to end in the following calendar year, unless terminated by the participant as provided in Section 10 hereof.

(e) At the time the option is exercised, in whole or in part, or at the time some or all of the Company's Common Stock issued under the Plan is disposed of, the participant must make adequate provision for the Company's federal, state, or other tax withholding obligations, if any, which arise upon the exercise of the option. If the participant makes a disposition, within the meaning of Section 424(c) of the Code and regulations promulgated thereunder, of any shares of Common Stock issued to such participant pursuant to the exercise of an option, and such disposition occurs within the two-year period commencing on the day after the Offering Date or within the one-year period commencing on the day after the exercise date, such participant shall, within five (5) days of such disposition, notify the Company thereof. In addition, in order to satisfy the requirement to withhold the amount (if any) of federal, state or local taxes that the Company or Subsidiary determines is applicable, the Company and any Subsidiary may deduct such amount from any other compensation payable to the Participant.

**7. Grant of Option.** On the Enrollment Date of each Offering Period, each Employee participating in such Offering Period shall be granted an option to purchase on each Exercise Date during such Offering Period (at the applicable Purchase Price) up to a number of shares of the Company's Common Stock determined by dividing such Employee's payroll deductions accumulated prior to such Exercise Date and retained in the participant's account as of the Exercise Date by the applicable Purchase Price; provided that in no event shall an Employee be permitted to purchase during each Purchase Period more than Six Hundred Twenty Five (625) shares of the Company's Common Stock (subject to any adjustment pursuant to Section 19), and provided further that such purchase shall be subject to the limitations set forth in Sections 3(b) and 12 hereof. The Board or the Committee may, for future Offering Periods, increase or decrease, in its absolute discretion, the maximum number of shares of the Company's Common Stock an Employee may purchase during each Purchase Period of such Offering Period. Exercise of the option shall occur as provided in Section 8 hereof, unless the participant has withdrawn pursuant to Section 10 hereof. The option shall expire on the last day of the Offering Period.

**8. Exercise of Option.**

(a) Unless a participant withdraws from the Plan as provided in Section 10 hereof, his or her option for the purchase of shares shall be exercised automatically on the Exercise Date, and the maximum number of full shares subject to the option shall be purchased for such participant at the applicable Purchase Price with the accumulated payroll deductions in his or her account. No fractional shares shall be purchased; any payroll deductions accumulated in a participant's account which are not sufficient to purchase a full share shall be retained in the participant's account for the subsequent Purchase Period or Offering Period, subject to earlier

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withdrawal by the participant as provided in Section 10 hereof. Any other monies left over in a participant's account after the Exercise Date shall be returned to the participant. During a participant's lifetime, a participant's option to purchase shares hereunder is exercisable only by him or her.

(b) If the Board or the Committee determines that, on a given Exercise Date, the number of shares with respect to which options are to be exercised may exceed (i) the number of shares of Common Stock that were available for sale under the Plan on the Enrollment Date of the applicable Offering Period, or (ii) the number of shares available for sale under the Plan on such Exercise Date, the Board may in its sole discretion (x) provide that the Company shall make a pro rata allocation of the shares of Common Stock available for purchase on such Enrollment Date or Exercise Date, as applicable, in as uniform a manner as shall be practicable and as it shall determine in its sole discretion to be equitable among all participants exercising options to purchase Common Stock on such Exercise Date, and continue all Offering Periods then in effect, or (y) provide that the Company shall make a pro rata allocation of the shares available for purchase on such Enrollment Date or Exercise Date, as applicable, in as uniform a manner as shall be practicable and as it shall determine in its sole discretion to be equitable among all participants exercising options to purchase Common Stock on such Exercise Date, and terminate any or all Offering Periods then in effect pursuant to Section 20 hereof. The Company may make pro rata allocations of the shares available on the Enrollment Date of any applicable Offering Period pursuant to the preceding sentence, notwithstanding any authorization of additional shares for issuance under the Plan by the Company's stockholders subsequent to such Enrollment Date.

**9. Delivery.** As promptly as practicable after each Exercise Date on which a purchase of shares occurs, the Company shall arrange the delivery to each participant, as appropriate, the shares purchased upon exercise of his or her option in a certificate or uncertificated form.

### **10. Withdrawal.**

(a) A participant may withdraw all but not less than all the payroll deductions credited to his or her account and not yet used to exercise his or her option under the Plan at any time by giving written notice to Plan Administrator which is received at least ten (10) days prior to the Exercise Date (or such other notice period as may be established by the Plan Administrator from time to time in its sole discretion). All of the participant's payroll deductions credited to his or her account shall be paid to such participant promptly after receipt of notice of withdrawal and such participant's option for the Offering Period shall be automatically terminated, and no further payroll deductions for the purchase of shares shall be made for such Offering Period. If a participant withdraws from an Offering Period, payroll deductions shall not resume at the beginning of the succeeding Offering Period unless the participant delivers to the Plan Administrator a new Authorization Form.

(b) A participant's withdrawal from an Offering Period shall not have any effect upon his or her eligibility to participate in any similar plan that may hereafter be adopted by the Company or in succeeding Offering Periods that commence after the termination of the Offering Period from which the participant withdraws.

**11. Termination of Employment.** Upon a participant's ceasing to be an Employee, for any reason, he or she shall be deemed to have elected to withdraw from the Plan and the payroll deductions credited to such participant's account during the Offering Period but not yet used to exercise the option shall be returned to such participant or, in the case of his or her death, to the person or persons entitled thereto under Section 15 hereof, and such participant's option shall be automatically terminated.

**12. Interest.** No interest shall accrue on the payroll deductions of a participant in the Plan.

### **13. Stock.**

(a) Subject to adjustment upon changes in capitalization of the Company as provided in Section 19 hereof, the maximum number of shares of the Company's Common Stock which shall be made available for sale under

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the Plan with respect to Exercise Dates (including Exercise Dates with respect to outstanding Offering Periods under the Prior Plan and ones with respect to Offering Periods commencing under the Plan) shall be One Million Five Hundred Thousand (1,500,000) shares, effective as of the date of the effective date of the Plan.

(b) The participant shall have no interest or voting rights in shares covered by his or her option until such option has been exercised.

(c) Shares to be delivered to a participant under the Plan shall be registered in the name of the participant or in the name of the participant and his or her spouse.

**14. Administration.** The Committee shall mean the Compensation Committee of the Board, a subcommittee thereof formed by the Compensation Committee to act as the Committee hereunder or such other committee of members of the Board as delegated by the Board. The Board or the Committee shall administer the Plan. The Board or the Committee shall have full and exclusive discretionary authority to construe, interpret and apply the terms of the Plan, to determine eligibility and to adjudicate all disputed claims filed under the Plan. Every finding, decision and determination made by the Board or the Committee shall, to the full extent permitted by law, be final and binding upon all parties. The Company will pay all expenses incurred in the administration of the Plan. No member of the Committee or individual acting on behalf of the Plan Administrator shall be personally liable for any action, determination, or interpretation made in good faith with respect to the Plan, and all members of the Committee and individuals acting on behalf of the Plan Administrator shall be fully indemnified by the Company with respect to any such good faith action, determination or interpretation.

## **15. Designation of Beneficiary.**

(a) A participant may file with the Plan Administrator a written designation of a beneficiary who is to receive any shares and cash from the participant's account under the Plan in the event of such participant's death subsequent to an Exercise Date on which the option is exercised but prior to delivery to such participant of such shares and cash. In addition, a participant may file with the Plan Administrator a written designation of a beneficiary who is to receive any cash from the participant's account under the Plan in the event of such participant's death prior to the exercise of the option. If a participant is married and the designated beneficiary is not the spouse, spousal consent shall be required for such designation to be effective.

(b) Such designation of beneficiary may be changed by the participant at any time by written notice to the Plan Administrator. In the event of the death of a participant and in the absence of a beneficiary validly designated under the Plan who is living at the time of such participant's death, the Company shall deliver such shares and/or cash to the executor or administrator of the estate of the participant, or if no such executor or administrator has been appointed (to the knowledge of the Company), the Company, in its discretion, may deliver such shares and/or cash to the spouse or to any one or more dependents or relatives of the participant, or if no spouse, dependent or relative is known to the Company, then to such other person as the Company may designate.

**16. Transferability.** Neither payroll deductions credited to a participant's account nor any rights with regard to the exercise of an option or to receive shares under the Plan may be assigned, transferred, pledged or otherwise disposed of in any way (other than by will, the laws of descent and distribution or as provided in Section 15 hereof) by the participant. Any such attempt at assignment, transfer, pledge or other disposition shall be without effect, except that the Company may treat such act as an election to withdraw funds from an Offering Period in accordance with Section 10 hereof.

**17. Use of Funds.** All payroll deductions received or held by the Company under the Plan may be used by the Company for any corporate purpose, and the Company shall not be obligated to segregate such payroll deductions.

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**18. Reports.** Individual accounts shall be maintained for each participant in the Plan. Statements of account shall be given to participating Employees at least annually, which statements shall set forth the amounts of payroll deductions, the Purchase Price, the number of shares purchased and the remaining cash balance, if any.

## **19. Adjustments Upon Changes in Capitalization, Dissolution, Liquidation, Merger or Asset Sale.**

(a) *Changes in Capitalization.* Subject to any required action by the stockholders of the Company, the Reserves, the maximum number of shares each participant may purchase each Purchase Period (pursuant to Section 7), as well as the price per share and the number of shares of Common Stock covered by each option under the Plan which have not yet been exercised shall be proportionately adjusted for any increase or decrease in the number of issued shares of Common Stock resulting from a stock split, reverse stock split, stock dividend, extraordinary cash dividend, combination or reclassification of the Common Stock, or any other increase or decrease in the number of shares of Common Stock effected without receipt of consideration by the Company; provided, however, that conversion of any convertible securities of the Company shall not be deemed to have been effected without receipt of consideration. Such adjustment shall be made by the Board or the Committee, whose determination in that respect shall be final, binding and conclusive. Except as expressly provided herein, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock subject to an option.

(b) *Dissolution or Liquidation.* In the event of a proposed dissolution or liquidation of the Company, the Offering Period then in progress shall be shortened by setting a new Exercise Date (the New Exercise Date), and shall terminate immediately prior to the consummation of such proposed dissolution or liquidation, unless provided otherwise by the Board. The New Exercise Date shall be before the date of the Company's proposed dissolution or liquidation. The Board shall notify each participant in writing, at least ten (10) business days prior to the New Exercise Date, that the Exercise Date for the participant's option has been changed to the New Exercise Date and that the participant's option shall be exercised automatically on the New Exercise Date, unless prior to such date the participant has withdrawn from the Offering Period as provided in Section 10 hereof.

(c) *Merger or Asset Sale.* In the event of a proposed sale of all or substantially all of the assets of the Company, or the merger of the Company with or into another corporation, each outstanding option shall be assumed or an equivalent option substituted by the successor corporation or a parent or subsidiary of the successor corporation. In the event that the successor corporation refuses to assume or substitute for the option, any Purchase Periods then in progress shall be shortened by setting a new Exercise Date (the New Exercise Date) and any Offering Periods then in progress shall end on the New Exercise Date. The New Exercise Date shall be before the date of the Company's proposed sale or merger. The Board shall notify each participant in writing, at least ten (10) business days prior to the New Exercise Date, that the Exercise Date for the participant's option has been changed to the New Exercise Date and that the participant's option shall be exercised automatically on the New Exercise Date, unless prior to such date the participant has withdrawn from the Offering Period as provided in Section 10 hereof.

## **20. Amendment or Termination.**

(a) The Board may at any time and for any reason terminate or amend the Plan. Except as provided in Section 19 hereof, no such termination can affect options previously granted, provided that an Offering Period may be terminated by the Board on any Exercise Date if the Board determines that the termination of the Offering Period or the Plan is in the best interests of the Company and its stockholders. Except as provided in Section 19 and this Section 20 hereof, no amendment may make any change in any option theretofore granted which adversely affects the rights of any participant. To the extent necessary to comply with Section 423 of the Code (or any successor rule or provision or any other applicable law, regulation or rule of the NASDAQ Stock Market or such other principal U.S. national securities exchange Common Stock is listed), the Company shall obtain stockholder approval in such a manner and to such a degree as required.

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(b) Without stockholder approval and without regard to whether any participant rights may be considered to have been adversely affected, the Board or the Committee shall be entitled to change the Offering Periods, limit the frequency and/or number of changes in the amount withheld during an Offering Period, establish the exchange ratio applicable to amounts withheld in a currency other than U.S. dollars, permit payroll withholding in excess of the amount designated by a participant in order to adjust for delays or mistakes in the Company's processing of properly completed withholding elections, establish reasonable waiting and adjustment periods and/or accounting and crediting procedures to ensure that amounts applied toward the purchase of Common Stock for each participant properly correspond with amounts withheld from the participant's Compensation, and establish such other limitations or procedures as the Board or the Committee determines in its sole discretion advisable which are consistent with the Plan.

(c) In the event the Board determines that the ongoing operation of the Plan may result in unfavorable financial accounting consequences, the Board may, in its discretion and, to the extent necessary or desirable, modify or amend the Plan to reduce or eliminate such accounting consequences including, but not limited to:

- (1) altering the Purchase Price for any Offering Period including an Offering Period underway at the time of the change in Purchase Price;
- (2) shortening any Offering Period so that the Offering Period ends on a new Exercise Date, including an Offering Period underway at the time of the Board action; and
- (3) allocating shares.

Such modifications or amendments shall not require stockholder approval or the consent of any Plan participants.

**21. Notices.** All notices or other communications by a participant to the Company under or in connection with the Plan shall be deemed to have been duly given when received in the form specified by the Company at the location, or by the person, designated by the Company for the receipt thereof.

**22. Conditions Upon Issuance of Shares.** Shares shall not be issued with respect to an option unless the exercise of such option and the issuance and delivery of such shares pursuant thereto shall comply with all applicable provisions of law, domestic or foreign, including, without limitation, the Securities Act of 1933, as amended, the Securities Exchange Act of 1934, as amended, the rules and regulations promulgated thereunder, and the requirements of the NASDAQ Stock Market (or any other principal U.S. national securities exchange on which the Common Stock may then be listed), and shall be further subject to the approval of counsel for the Company with respect to such compliance. As a condition to the exercise of an option, the Company may require the person exercising such option to represent and warrant at the time of any such exercise that the shares are being purchased only for investment and without any present intention to sell or distribute such shares if, in the opinion of counsel for the Company, such a representation is required by any of the aforementioned applicable provisions of law.

**23. Term of Plan.** The Plan shall become effective upon its approval by the stockholders of the Company and shall continue in effect until June 25, 2019, unless sooner terminated under Section 20 hereof.

**24. Miscellaneous.**

(a) *Administrative Costs.* The Company shall pay the administrative expenses associated with the operation of the Plan (other than brokerage commissions resulting from sales of Common Stock directed by Employees).

(b) *No Employment Rights.* Participation in the Plan shall not give an Employee any right to continue in the employment of the Company, and shall not affect the right of the Company to terminate the Employee's employment at any time, with or without cause.

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(c) *Repurchase of Stock.* The Company shall not be required to purchase or repurchase from any Employee any of the shares of Common Stock that the Employee acquires under the Plan.

(d) *Internal Revenue Code and ERISA Considerations.* The Plan is intended to constitute an employee stock purchase plan within the meaning of section 423 of the Internal Revenue Code of 1986, as amended, and the regulations thereunder. The provisions of the Plan, accordingly, shall be construed so as to comply with the requirements of that section of the Code or any successor provision, and the regulations thereunder. The Plan is not intended and shall not be construed as constituting an employee benefit plan, within the meaning of section 3(3) of the Employee Retirement Income Security Act of 1974, as amended.

(e) *Headings, Captions, Gender.* The headings and captions herein are for convenience of reference only and shall not be considered as part of the text. The masculine shall include the feminine, and vice versa.

(f) *Severability of Provisions, Prevailing Law.* The provisions of the Plan shall be deemed severable. If any provision of the Plan shall be held unlawful or otherwise invalid or unenforceable in whole or in part by a court of competent jurisdiction or by reason of a change in a law or regulation, such provision shall (a) be deemed limited to the extent that such court of competent jurisdiction deems it lawful, valid and/or enforceable and as so limited shall remain in full force and effect, and (b) not affect any other provision of the Plan or part thereof, each of which shall remain in full force and effect. The Plan shall be governed by the laws of the State of California to the extent such laws are not in conflict with, or superseded by, federal law.

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**Arena Pharmaceuticals, Inc.**

C123456789

MR A SAMPLE	000004	00000000.000000 ext	00000000.000000 ext
DESIGNATION (IF ANY)		00000000.000000 ext	00000000.000000 ext
ADD 1		00000000.000000 ext	00000000.000000 ext
ADD 2			
ADD 3			
ADD 4			
ADD 5			
ADD 6			

**Electronic Voting Instructions**  
**You can vote by Internet or telephone!**  
**Available 24 hours a day, 7 days a week!**

Instead of mailing your proxy, you may choose one of the two voting methods outlined below to vote your proxy.

VALIDATION DETAILS ARE LOCATED BELOW IN THE TITLE BAR.  
**Proxies submitted by the Internet or telephone must be received by 11:00 p.m. Pacific Time on June 24, 2009.**

**Vote by Internet**

Log on to the Internet and go to **www.investorvote.com/ARNA**  
Follow the steps outlined on the secured website.

**Vote by telephone**

Call toll free 1-800-652-VOTE (8683) within the United States, Canada & Puerto Rico any time on a touch tone telephone. There is **NO CHARGE** to you for the call.

Follow the instructions provided by the recorded message.

Using a **black ink** pen, mark your votes with an **X** as shown in this example. Please do not write outside the designated areas.

**X**

q IF YOU HAVE NOT VOTED VIA THE INTERNET OR TELEPHONE, FOLD ALONG THE PERFORATION, DETACH AND RETURN THE BOTTOM PORTION IN THE ENCLOSED ENVELOPE. q



**A** Proposals The Board of Directors recommends a vote **FOR** all the nominees listed in Proposal 1 and **FOR** Proposals 2 through 5.

1. Election of Directors: For Withhold For Withhold For Withhold

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01 - Jack Lief	..	..	02 - Dominic P. Behan, Ph.D.	..	..	03 - Donald D. Belcher	..	..	+
04 - Scott H. Bice	..	..	05 - Harry F. Hixson, Jr., Ph.D.	..	..	06 - J. Clayburn La Force, Jr., Ph.D.	..	..	
07 - Tina S. Nova, Ph.D.	..	..	08 - Phillip M. Schneider	..	..	09 - Christine A. White, M.D.	..	..	
10 - Randall E. Woods	..	..							

	For	Against	Abstain		For	Against	Abstain
2. Approval of the Arena Pharmaceuticals, Inc., 2009 Long-Term Incentive Plan.	..	..	..	3. Approval of the Arena Pharmaceuticals, Inc., 2009 Employee Stock Purchase Plan.	..	..	..
4. Approval of an amendment to Arena's Fifth Amended and Restated Certificate of Incorporation to increase the total number of authorized shares from 150.0 million to 250.0 million and the number of authorized shares of common stock from 142.5 million to 242.5 million.	..	..	..	5. Ratification of the appointment of Ernst & Young LLP, an independent registered public accounting firm, as Arena's independent auditors for the fiscal year ending December 31, 2009.	..	..	..

**B**

**Non-Voting Items**

**Change of Address** Please print new address below.

**Meeting Attendance**  
Mark box to the right if you plan to attend the Annual Meeting. ..

**IF VOTING BY MAIL, YOU MUST COMPLETE SECTIONS A - C ON BOTH SIDES OF THIS CARD.**

<STOCK#> 01238B

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¶ IF YOU HAVE NOT VOTED VIA THE INTERNET OR TELEPHONE, FOLD ALONG THE PERFORATION, DETACH AND RETURN THE BOTTOM PORTION IN THE ENCLOSED ENVELOPE. ¶

Proxy **Arena Pharmaceuticals, Inc.**

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**THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS FOR**

**THE 2009 ANNUAL MEETING OF STOCKHOLDERS**

**6154 Nancy Ridge Drive, San Diego, California 92121**

The undersigned stockholder of ARENA PHARMACEUTICALS, INC., a Delaware corporation (the Company), hereby acknowledges receipt of the Notice of Annual Meeting of Stockholders and Proxy Statement, each dated May 15, 2009, and the Annual Report to Stockholders, and hereby appoints Jack Lief and Steven W. Spector, the President and the Secretary, respectively, of the Company, or each of them, as proxies and attorneys-in-fact, with all powers of substitution, to represent and vote, as set forth on the reverse side, the shares of Common Stock of the Company held of record by the undersigned at the close of business on April 27, 2009, at the 2009 Annual Meeting of Stockholders of the Company, which is being held at the offices of the Company at 6154 Nancy Ridge Drive, San Diego, California 92121, on Thursday, June 25, 2009, at 9:00 a.m. Pacific Time, and at any adjournments or postponements of such meeting, with all powers which the undersigned would possess if personally present at such meeting or at any such postponement or adjournment, and, in their discretion, to vote such shares upon any other business that may properly come before the meeting or any adjournments or postponements thereof.

**UNLESS OTHERWISE SPECIFIED BY THE UNDERSIGNED, THE PROXY WILL BE VOTED FOR ALL OF THE NOMINEES LISTED IN PROPOSAL 1 AND FOR PROPOSALS 2 THROUGH 5 AND WILL BE VOTED BY THE PROXYHOLDERS AT THEIR DISCRETION UPON ANY OTHER BUSINESS THAT MAY PROPERLY COME BEFORE THE ANNUAL MEETING OR ANY ADJOURNMENT OR POSTPONEMENTS THEREOF.**

(Items to be voted appear on reverse side.)

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**C** Authorized Signatures This section must be completed for your vote to be counted. Date and Sign Below

NOTE: Please sign your name(s) EXACTLY as your name(s) appear(s) on this proxy. All joint holders must sign. When signing as attorney, trustee, executor, administrator, guardian or corporate officer, please provide your FULL title.

Date (mm/dd/yyyy) Please print date below.

Signature 1 Please keep signature within the box.

Signature 2 Please keep signature within the box.

/ /

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**IF VOTING BY MAIL, YOU MUST COMPLETE SECTIONS A - C ON BOTH SIDES OF THIS CARD.**

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